CLERK'S COPY.

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1932

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

vs.

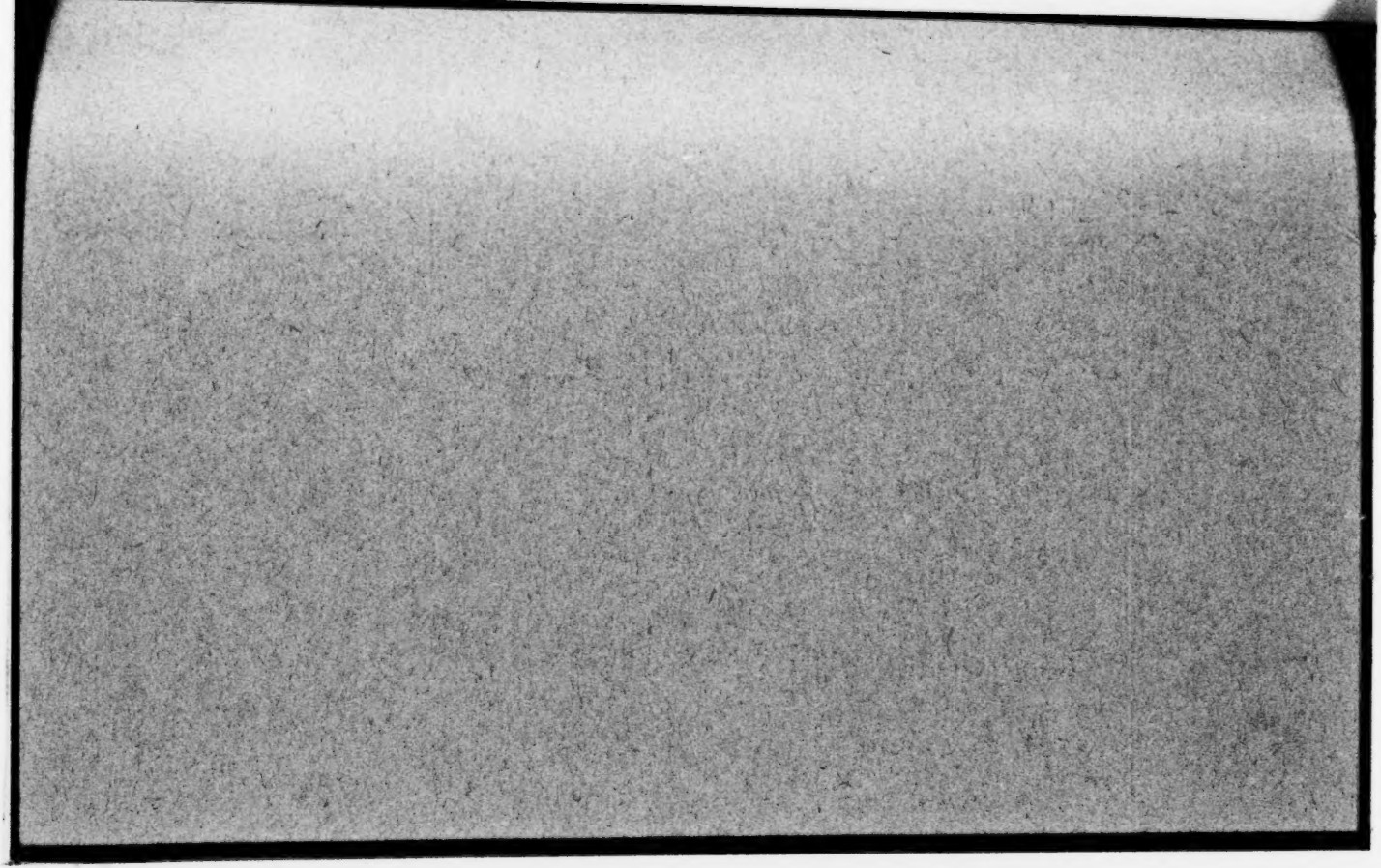
COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR CERTIORARI FILED MAY 23, 1932

CERTIORARI GRANTED OCTOBER 10, 1932

(36,801)



(36,801)

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1932

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

INDEX

	Page
Proceedings before U. S. Board of Tax Appeals	1
Docket entries #14516-17	1
Docket entries #42664	4
Petition #14517	5
Deficiency letter #14517	10
Answer #14517	15
Amended petition	18
Statement re petition, etc., #14516	21
Deficiency letter #14516	21
Statement re petition, etc., #42664	27
Deficiency letter #42664	27
Motion for consolidation	36
Findings of fact and opinion, Smith, M	37
Motion for rehearing and modification	57
Order denying motion for rehearing	59
Respondent's notice of settlement	61
Petitioner's objection and counter-proposal	66
Order denying motion for rehearing and reargument	69

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., OCTOBER 26, 1932

Page

Decision 70
Order amending findings 72
Petition for review 73
Statement of evidence 84
Testimony of D. J. F. Strother 84
Summary of Petitioner's Exhibit No. 1 88
Testimony of Judge Strother 99
Testimony of D. J. F. Strother (recalled) 103
Præcipe for transcript of record 111
Agreed order re single record 113
Certificate of clerk 116
Proceedings in United States circuit court of appeals, fourth circuit. 117
Docket entries 117
Opinion, Soper, J 119
Judgment 135
Petition for rehearing 137
Order denying rehearing 169
Motion for leave to file supplemental petition for rehearing 170
Supplemental petition for rehearing 171
Order denying rehearing and staying mandate 185
Clerk's certificate 186
Order allowing certiorari 187

TRANSCRIPT OF RECORD

Docket Nos. 14516-17

Appearances:

For Petitioner:
Camden R. McAtee, Esq.,

For Respondent:
M. E. McDowell, Esq.,
W. F. Gibbs, Esq.,
F. Schlosser, Esq.

Bankers Pocahontas Coal Company,
Petitioner,

vs.

Commissioner of Internal Revenue,
Respondent.

DOCKET ENTRIES

The entries in both appeals are identical and as follows:

1926

Apr. 24—Petition received and filed.
May 3—Copy of petition served on Solicitor.
May 3—Notification of receipt mailed taxpayer.
June 1—Answer filed by Solicitor.
June 24—Copy of answer served on taxpayer—General Calendar.

1927

Sept. 8—Motion to consolidate for hearing with dockets 18679, 18680, 26655-56, 10472, 25275 and 14516 filed by taxpayer. See 18679. Granted.

1928

June 27—Hearing set Sept. 11, 1928.
July 29—Motion for a continuance to Oct. 10, 1928 filed by taxpayer.
July 23—Motion granted.
July 31—Application for order to take depositions filed by taxpayer.
Oct. 9—Motion for a 60 day continuance filed by taxpayer. See 14516.
Oct. 11—Motion for a continuance to Dec. 10, 1928—granted.
Dec. 6—Motion for continuance to Feb. 15, 1929 filed by taxpayer.

1929

Jan. 28—Motion for a continuance to April 15, 1929 filed by taxpayer. Granted to Apr. 15, 1929.
Mar. 22—Motion for a continuance to 5/2/29 filed by taxpayer. 3/25/29 granted.
Apr. 27—Motion to consolidate with 14516 and 42664 and advance hearing of docket 42664 to 5/2/29 filed by taxpayer. See 14516.
Apr. 27—Motion for leave to amend petition filed by taxpayer—amended petition tendered—copy served 5/1.
Apr. 30—Motion for leave to amend petition granted.
May 2—Hearing had before Chas. P. Smith, Division 5, on merits—heard with 10472, 25275, 32170 and 42664.
May 20—Transcript of hearing May 2 and 3, 1929 filed.
July 17—Motion for extension of 30 days from Aug. 1st to file briefs (both parties) filed by General Counsel.
July 19—Motion granted.
Aug. 28—Brief filed by General Counsel.
Aug. 31—Motion for extension of 10 days to file brief filed by taxpayer.
Sept. 10—Requested findings of fact and brief filed by (2) taxpayer.

1930

Jan. 22—Findings of fact and opinion rendered, Mr. Smith, Division 5, judgment will be entered Rule 50.

Feb. 27—Motion for rehearing and modified findings of fact and opinion filed by taxpayer.
Mar. 6—Order denying motion of Feb. 27 for rehearing entered.
Mar. 31—Notice of settlement filed by General Counsel.
Apr. 3—Hearing set April 23, 1930.
Apr. 21—Motion to postpone hearing for 30 days filed by taxpayer. 4/22/30 granted to May 21st.
May 21—Objections to General Counsel's notice of settlement and counter-determination filed by taxpayer.
May 21—Hearing had before Mr. Smith on settlement under Rule 50. Continued to June 18, 1930.
May 21—Order of continuance to June 18, 1930 for hearing on settlement under Rule 50 entered.
May 24—Transcript of hearing of May 21, 1930 filed.
June 18—Hearing had before Mr. Smith, Division 5, proposed redetermination under Rule 50.
July 1—Transcript of hearing of June 18, 1930 filed.
July 15—Order denying motion for rehearing or argument entered.
July 16—Decision entered—C. P. Smith, Division 5.
Sept. 26—Order amending findings of fact promulgated Jan. 22, 1930 entered.

1931

Jan. 6—Petition for review to U. S. Circuit Court of Appeals, 4th Circuit, with assignments of error filed by taxpayer.
Feb. 28—Certified copy of order extending time for 60 days to settle statement and transmit record filed.
Apr. 24—Certified copy of order extending time for 60 days to settle statement and transmit record filed.
July 11—Certified copy of order from U. S. Circuit Court of Appeals (4th) to transmit single record to Court filed.
July 14—Agreed praecipe filed.
July 14—Agreed statement of evidence approved and ordered filed.

(3) Docket No. 42664

Appearances:

For Petitioner:
Camden R. McAtee, Esq.,

For Respondent:
M. E. McDowell, Esq.,
W. F. Gibbs, Esq.,
F. Schlosser, Esq.

Bankers Pocahontas Coal Company,
Petitioner,

vs.

Commissioner of Internal Revenue,
Respondent.

DOCKET ENTRIES

1929

Feb. 11—Petition received and filed. Taxpayer notified. (Fee paid)
Feb. 12—Copy of petition served on General Counsel.
Mar. 12—Answer filed by General Counsel.
Mar. 23—Copy of answer served on taxpayer—General Calendar.
Apr. 27—Motion to consolidate for hearing on May 2, 1929 with dockets 14516 and 14517 filed by taxpayer. 4/30/29 granted.
Apr. 27—Motion for leave to amend petition, amendment tendered, filed by taxpayer. See 14516.

After this date the entries are identical with entries in Appeals 14516, 14517 as appearing herein.

PETITION

(4) Filed April 24, 1926.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket No. 14517

Commisioner of Internal Revenue,
Respondent.

The above named petitioner hereby appeals from the determination of the Commissioner of Internal Revenue set forth in his deficiency letter (IT:CA:2332-4-60D), dated February 15, 1926, and as the basis of its appeal sets forth the following:

1. The petitioner is a West Virginia Corporation with its principal offices at Welch, West Virginia.

2. The deficiency letter was mailed to taxpayer February 15, 1926.

3. The taxes in controversy are income and profits taxes for the calendar year 1920, and are less than $10,000.00 in amount.

4. The determination of tax contained in said deficiency letter is based upon the following errors:

(a) For the year 1920 in the addition to gross income of items previously reported as taxable income for the (5) year 1919, to-wit: "Royalties—$5434.68" and "Taxes refunded—$180.00".

(b) For the year involved in this appeal in establishing a depletion unit, and in establishing an erroneous depletion unit.

(c) Disallowance of so-called depletion and increase

of income thereby for the year as follows, to wit: 1920—$29,401.36.

(d) Reduction of invested capital by pro-rating dividends for each of the several years as follows, to wit: 1920—$12,630.33.

(e) Adjustment of surplus with reference to invested capital for each of the several years as follows, to wit: 1920—$32,015.22.

5. The facts upon which the petitioner relies as the basis of its appeal are as follows:

(a) Prior to March 1, 1913, the owner of, or owners of, the fee simple title of certain lands in West Virginia containing coal, and which lands were without value except for their coal content, had by written agreements with third parties divested themselves of ownership and control of said coal content and effected a sale of same in place. The purchasers thereof had taken actual and continuous possession of the respective properties, were mining the coal therefrom, and paying to the original owner thereof the considerations provided in said written instruments. Said written instruments were (6) and are in form and substance the same as is shown by specimen copy filed herein as part hereof, marked "Exhibit 2".

(b) In the year 1912 petitioner corporation was duly organized and acquired the fee simple title to the lands aforesaid, which were then and are now without value except for their coal content, and by assignment also acquired the rights and interest of the predecessor owner or owners in the written instruments aforesaid, but did not acquire or obtain title to the coal content of said lands previously sold and disposed of as aforesaid. Since its organization, petitioner has done no business except the receipt of payments provided for in said written instruments to be paid by the parties extracting the coal content from said lands, and the distribution of same to its stockholders.

(c) Petitioner states that since its organization in

1912, it has not been, and is not the owner of any mine or mines nor the lessor thereof, but in fact has been and is the owner of choses in action or contracts from which its entire income is derived.

(d) Petitioner states that its right or claim to collect the payments provided in said written instruments existed unconditionally on March 1, 1913, and was owned and held by petitioner prior to said date and the payments therein provided and received subsequent to March
(7) 1, 1913, and particularly in the calendar years 1919 to 1923, inclusive, do not constitute taxable income to petitioner.

(e) Petitioner states it is consistent with the natural adaptation of mineral property, and particularly of coal in place, that different parties should own the surface and the underlying minerals, and that by conveyance or appropriate written instrument a complete severance of title and separate estates may be and is created, and that same was effected as to the sale of coal in place hereinabove described.

(f) Petitioner states it is not a lessor as defined in regulations of the Bureau of Internal Revenue, and its alleged depletion allowance for the several taxable years has been and is erroneously and illegally computed as though petitioner was and is a lessor; that heretofore, misconceiving its proper status, petitioner reported taxable net income and permitted taxes to be assessed thereon with petitioner considered as a lessor, which was and is erroneous; that, in fact, petitioner in receiving the so-called royalties provided for in the aforesaid written instruments, has only received payments from year to year upon a claim or chose in action existing unconditionally on or before March 1, 1913, and such payments are non-taxable income to petitioner for each of the years when received.

(g) Specifically, in support of its allegations of error
(8) in said deficiency letter, petitioner further says:

(h) That its return of income for the several years has been made upon a cash receipt and disbursement basis, including in each year the income attributable to

same; that its payments under said written instruments are due each month, but do not come to hand until the subsequent month or months; that petitioner included in its 1919 return of income payments due in 1919, but not actually shown upon its books until January and February 1920, in the amount of $5,434.66 and an income tax refund of $180.00, which was likewise not entered on its books until January, 1920; that the adjustment proposed in the deficiency letters of February 12, 1926, and February 15, 1926, including said items in 1920 income, is contrary to established accounting methods of petitioner and causes petitioner to report same a second time as taxable income.

(i) That attempted depletion adjustments and the errors of same, in that petitioner is not a lessor, have been hereinabove fully stated.

(j) That the pro-rating of dividends with consequent adjustment of invested capital for the year 1920 is contrary to law, as determined by this honorable Board.

(k) That adjustments of surplus for said year with consequent effect upon invested capital is erroneous (9) as including income and profits taxes and appreciation incorrectly computed by reason of other errors hereinabove alleged.

II.

In the alternative, but without admitting same is right or proper, petitioner states if its status be determined herein to be that of a lessor subject to depletion allowances in determination of its taxable net income and tax liability, petitioner alleges and charges the depletion unit used in said deficiency letter is erroneous and insufficient in that same is not based upon the true and correct recoverable coal content and value thereof as existing on March 1, 1913; that all seams of coal and their content and quality were not considered in determining said coal content or value; that the alleged original coal used in determining alleged appreciation realized before March 1, 1913, as determined is insufficient and erroneous and is not the true and correct cost to petitioner of the assets considered.

On the hearing of this appeal petitioner will introduce evidence intended to show the alleged depletion unit assigned for petitioner in the computation of its taxable net income was and is erroneous as aforesaid, provided said issue is found to be material to the proper determination of its taxes in this proceeding.

6. The taxpayer in support of its appeal relies upon
(10) the following propositions of law:

(a) The method of accounting regularly employed by taxpayer in keeping its books and clearly reflecting its income is to be followed with respect to the time as to which items of gross income and deductions are to be accounted for.

(b) Property held by taxpayer on March 1, 1913, including claims or choses in action, is capital.

(c) In the case of mines a reasonable allowance for depletion shall be allowed as a deduction from gross income in computing net income.

(d) Invested capital may not be reduced in determining the extent to which a dividend is paid from current earnings of the taxable year by a theoretical tentative tax set aside out of current earnings and pro-rated over such year, because income and profits taxes do not become due and payable, and hence do not accrue, until the following year.

WHEREFORE, the premises considered, petitioner respectfully prays that this Board may hear and determine its appeal.

(s) CAMDEN R. McATEE
Counsel for Petitioner,
Woodward Building,
Washington, D. C.

State of West Virginia,
(11) County of McDowell, ss:

D. J. F. Strother, being duly sworn, says that he is President of the Bankers Pocahontas Coal Company,

above named, and as such is duly authorized to verify the foregoing petition; that he had read the said petition, and is familiar with the statements therein continued and that the facts therein stated are true, except such facts as are stated to be upon information and belief, and those facts he believes to be true.

(s) D. J. F. STROTHER

Subscribed and sworn to before me this 22nd day of April, 1926.

(s) RUBY SLEDGE REYBURN
Notary Public.

My Commission expires Dec. 11, 1934.

Commissioned as Ruby Sledge.

(12) Form NP-2

TREASURY DEPARTMENT

Washington

(COPY)

Feb. 15, 1926.

IT:CA:2332-4-60D

Bankers Pocahontas Coal Co.,
Welch, West Virginia.

Sirs:

The determination of your income and profits tax liability for the year 1920 has been reconsidered in connection with an examination of your books of account and records and a conference held in the Unit January 4, 1926, and a deficiency in the amount of $6,797.56 has been disclosed as shown in the attached statement.

In accordance with the provisions of Section 274 of

the Revenue Act of 1924, you are allowed 60 days from the date of mailing of this letter within which to file an appeal contesting in whole or in part the correctness of this determination. Any such appeal must be addressed to the United States Board of Tax Appeals, Washington, D. C., and must be mailed in time to reach that Board within the 60-day period.

Where a taxpayer has been given an opportunity to appeal to the Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has appealed and an assessment in accordance with the final decision on such appeal has been made, no claim in abatement in respect of any part of the deficiency will be entertained.

If you acquiesce in this determination and do not desire to file an appeal, you are requested to sign the enclosed agreement consenting to the assessment of the deficiency and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:CA: 2332-4-60D. In the event that you acquiesce in a part of the determination, the agreement should be executed with respect to the items agreed to.

Respectfully,

D. H. BLAIR,
Commissioner.
By (S) C. R. NASH,
Assistant to the Commissioner.

Enclosures:

Statements
Agreement—Form A.
Form 882.

(13) STATEMENT

IT:CA:2332-4. February 15, 1926.

In re: Bankers Pocahontas Coal Company,
Welch, West Virginia.

1920

Deficiency in tax—$6,797.56.

ADJUSTMENTS TO INCOME

Net income reported on return			$10,114.34
Additions:			
1. Royalties, revenue agent's report		$63,706.66	
Royalties, return		58,272.00	5,434.66
2. Taxes refunded, revenue agent's report		$6,040.06	
Taxes refunded		5,860.06	180.00
3. Depletion, return	$45,773.01		
Depletion, revenue agent's report	16,371.65		29,401.36
Total			$45,130.36
Deduction:			
4. Interest Liberty Bonds			222.50
Net income corrected			$44,907.86

EXPLANATION OF ADJUSTMENTS TO NET INCOME

1. Royalties added to 1919 instead of 1920.

2. Taxes refunded in 1920 added to 1919 income.

3. Depletion as computed in the revenue agent's report, a copy of which was furnished you, has been accepted by this office.

4. Interest on Liberty Bonds of $222.50 is exempt.

INVESTED CAPITAL

Capital stock on revenue Agent's report		$150,000.00
Surplus, revenue agent's report		32,015.22
1. Undervaluation of coal lands		134,497.80
		$316,513.02

(14)

Deductions:		
2. Preceding year's tax, 1919 $3,386.04, prorated,	$ 1,427.05	
3. Dividends	7,500.00	
4. Dividends	12,630.33	21,557.38
Invested capital full year		$294,955.64

EXPLANATION OF ADJUSTMENTS TO INVESTED CAPITAL

1. The adjustment of invested capital for undervaluation of coal lands is based on data on file in this office.

2. Federal income taxes are deemed to have been paid out of the net income of a taxable year for which they are levied and, accordingly, may be included in the computation of invested capital only until such taxes become due and payable. The correct tax liability for the preceding taxable year has, therefore, been prorated from the due date in accordance with Article 845, Regulations 45.

3. Dividends paid during the first sixty days of the taxable year are deemed to have been paid from earnings accumulated during preceding years and have, accordingly, been prorated in accordance with Article 858, Regulations 45.

4. Dividends paid after the expiration of the first sixty days of the taxable year will be deemed to be paid out of the net income available for such purpose on the date when it is payable in accordance with Articles 857 and 858, Regulations 62.

DEDUCTION FOR DIVIDENDS

Available earnings for year		44,907.86
Tentative tax for year		7,296.95
Amount available for dividends		$37,610.91
Dividends paid March 31,		$ 7,500.00
Earnings for ninety days		$ 9,248.58
Dividends paid May 10		$22,500.00
Earnings for forty days	$4,110.48	
Plus	1,748.58	5,859.06
Paid from surplus		$16,640.94
Prorated for 236 days		$10,730.22

(15)

Dividends paid June 30	$,9000.00
Earnings for fifty-one days	5,240.86
Paid from surplus	$3,759.14
Prorated for 185 days	$1,900.11

Computation of Tax.

Invested capital	$294,955.64
Excess profits credit	$ 26,596.45
Excess profits tax	$ 3,662.28
Total profits tax	$ 3,662.28

Net income		$44,907.86	
Less: Profits tax	$3,662.28		
Exemption	2,000.00	5,682.28	
Balance taxable at 10%		$39,245.58	
Amount of tax at 10%			$3,924.56
Total tax assessable			$7,586.84
Original tax			$ 789.28
Deficiency in Tax			$6,797.56

Cletus Lease Exhibit omitted because same appears in Board's Findings.

ANSWER

(16) Filed June 1, 1926.

UNITED STATES BOARD OF TAX APPEALS

In re: Appeal of Bankers Pocahontas Coal Co., Welch, West Virginia

Docket No. 14517

Comes now the Commissioner of Internal Revenue, by his attorney A. W. Gregg, General Counsel, Bureau of Internal Revenue, and for answer to the petition filed in the above-entitled appeal, admits and denies as follows:

1. Admits the statements contained in paragraph 1 of the petition.

2. Admits the statements contained in paragraph 2 of the petition.

3. Admits the statements contained in paragraph 3 of the petition.

4. Denies that the determination of the Commissioner contains errors; and more particularly, that it contains those errors, specified in paragraph 4, subdivisions (a) to (e) inclusive.

5.(a) Admits that prior to March, 1, 1913 certain owners of the fee simple title of certain lands in West Virginia containing coal, had entered into written agreements of the character shown in taxpayer's Exhibit 2 and more particularly described as the "Cletus Lease"; but denies that said lands were without value except for their coal contents and denies further that the owners (17) of said lands had by said written contract divested themselves of ownership and control of said coal content and had effected a sale of the coal in place.

(b) Admits that the taxpayer corporation was organized in 1912; that it acquired the fee simple title to certain lands aforementioned; that by assignment it also acquired the rights and interest of the predecessor owner or owners in the written instruments aforementioned; but denies that said lands were without value except for their coal contents; denies that the taxpayer did not acquire or obtain title to the coal content of said lands; and denies that since its organization petitioner has done no business except to receive payments provided for in said written instruments and to distribute the same to its stockholders.

(c) Denies the statements contained in paragraph 5, subdivision (c) of the petition.

(d) Denies the statements contained in paragraph 5, subdivision (d) of the petition.

(e) Admits the statements contained in paragraph 5, subdivision (e) of the petition, except it is denied that the contracts here in question effected a sale of coal in place on the lands covered by said contracts heretofore mentioned.

(f) Denies the statements contained in paragraph 5, subdivision (f) except it is admitted that the taxpayer reported income and permitted certain Federal income (18) and profits taxes thereon to be computed upon the basis that it was a lessor of coal lands.

(h) Admits that the taxpayer returned its income upon the cash receipts and disbursements basis; that

it included in income for the year 1919 the amounts of $5,434.66 and refund of taxes of $180.00, which items were not entered on the taxpayer's books until January 1920; and admits that the Commissioner has included both of these items in income for 1920 rather than as income for 1919; but denies that that action is contrary to established accounting methods or that it requires the taxpayer to report the same the second time as taxable income.

(i) Admits that the depletion adjustments and the alleged errors thereon have, to a certain extent, been set out above but denies the conclusion that the petitioner is not a lessor.

(j) Denies the statements contained in paragraph 5, subdivision (j) of the petition.

(k) Denies the statements contained in paragraph 5, subdivision (k) of the petition.

II.

Denies that the depletion unit used by the Commissioner in the deficiency letter is erroneous or that its use results in the allowance of insufficient depletion.

Denies further that the recoverable coal content and value thereof as existing on March 1, 1913 were not (19) correctly determined by the Commissioner or that the Commissioner's determination thereof did not consider all seams of coal and their content and quality as of March 1, 1913.

WHEREFORE, it is prayed that the taxpayer's petition be dismissed and the appeal denied.

A. W. GREGG,
General Counsel,
Bureau of Internal Revenue.

OF COUNSEL:

WARD LOVELESS, Special Attorney.
Bureau of Internal Revenue.

WL/mvb

AMENDED PETITION

(20) Filed April 30, 1929.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket No. 14516 14517 42664

Commissioner of Internal Revenue,
Respondent.

For amended petition herein, petitioner, Bankers Pocahontas Coal Company, respectfully states as follows:

1. That heretofore for the calendar years 1914 to 1919, inclusive, the respondent, Commissioner of Internal Revenue, did assess against petitioner additional income taxes under the several Revenue Acts applicable to said years and each of them, and did require petitioner to pay the amount of said additional assessment to wit: $6,267.08, to Albert B. White, Collector of Internal Revenue at Parkersburg, West Virginia, which payment was made by petitioner under protest on August 17, 1921; that in the computation of said additional taxes, which were income and profits taxes, the respondent Commissioner of Internal Revenue, did compute the depletion unit allowable to the petitioner in each of said several years to be .036¢ per ton of coal produced.

2. That thereafter on or about February 15, 1923,
(21) petitioner after filing a claim for refund of said taxes, and having same rejected, instituted its action at law in the United States District Court for the Northern District of West Virginia to recover from said Albert B. White, Collector, the aforesaid amount of $6,267.08 of taxes as being illegally and erroneously collected, which action was thereafter by consent of the parties, transferred to the District Court for the Southern District of West Virginia, and in said Court proceeded to hearing and final judgment; that in said action the deple-

tion unit allowable under the several Revenue Acts to petitioner in the computation of the taxable net income, was put in issue and was litigated between the parties and said cause was submitted to the Court for its judgment upon an agreed statement of facts, including evidence as to said depletion unit and its proper amount; that thereafter, said Court being advised, gave its opinion that said depletion unit, which respondent had computed to be $.036 was erroneous and a depletion unit of $.05 for each of said years was allowable to petitioner in the computation of its taxes in controversy; that pursuant to said opinion the judgment of the Court was duly entered, awarding a recovery from the defendant, Albert B. White, Collector, in favor of petitioner of taxes (22) erroneously collected in the amount of $5,373.01 principal, interest and costs, and in the computation thereof the depletion unit, or capital value, existing on March 1, 1913 and to be excluded from gross income in the computation of taxable net income for the several years, was computed at $.05 per ton of coal produced and not at $.036 per ton as originally determined by respondent Commissioner; that said judgment was thereafter duly paid to petitioner as plaintiff in said action by the United States, and no appeal therefrom was taken, and said judgment has been and remains in full force and effect.

3. That in the action aforesaid, and herein, the parties are identical, being petitioner as plaintiff suing in its own right, and the United States as defendant, represented respectively by its Collector of Internal Revenue, and by the respondent, Commissioner of Internal Revenue; that said action was defended for the United States by the United States District Attorney, and by Robert A. Littleton, Special Attorney from the Office of the General Counsel of the Commissioner of Internal Revenue, which was known at said time as the Solicitor's office, as attorneys of record and the details of defense and satisfaction of said judgment were handled by said Special Attorney, or attorneys representing the respondent herein. That said Court had jurisdiction over the (23) parties and subject matter of said action, and that the depletion unit allowable to petitioner in the years in controversy in said action, being the capital value existing in the coal content of petitioner's property as of March 1, 1913, was and is the same subject

matter in controversy herein with respect to said depletion unit, and that said depletion unit was and is determined between the parties in the aforesaid action, and by the judgment of the Court entered therein.

That said judgment of the United States District Court for the Southern District of West Virginia, entered and in effect as aforesaid, was given upon the same cause of action concerning the depletion unit as aforesaid and now sought to be litigated herein, and petitioner pleads and relies upon the said judgment and the proceedings in the aforesaid action as res adjudicata as to the depletion unit herein; that under the provisions of Article 4, Section 1 of the Constitution of the United States, full faith and credit must be given in this proceeding to said judgment and judicial proceedings of said United States District Court existing as aforesaid.

4. And petitioner further states that at the hearing of this appeal, profert will be made of the record and
(24) judgment aforesaid, in support of the allegations of this amended petition.

WHEREFORE, petitioner prays as in its original petition and for all other proper relief to which it may be entitled.

(s) CAMDEN R. McATEE,
Counsel for Petitioner.

State of West Virginia,
(25) County of McDowell, ss:

D. J. F. Strother, being duly sworn, deposes and says that he is president of the Bankers Pocahontas Coal Company, a corporation, and authorized to make this affidavit; that he is familiar with the statements in the amended petition, and same are true as he verily believes.

(s) D. J. F. STROTHER.

Subscribed and sworn to before me this 20th day of April, 1929.

(s) RUBY SLEDGE REYBURN.
(Seal) Notary Public.

Commissioned as Ruby Sledge.

Commission expires Dec. 11, 1934.

(26) **STATEMENT**

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket No. 14516.

Commissioner of Internal Revenue,
Respondent.

The petition, amended petition, answer and Cletus Lease Exhibit herein are identical in substance with same in Appeal 14517, as affecting adjustments and deficiencies herein contested for the calendar years 1921, 1922 and 1923, excepting as to special incidental issues removed from controversy by the subsequent Board findings and opinion, and same are therefore here omitted, excepting the deficiency letter, which is as follows:

COPY

(27) Docket #14516

Form-NP-2

TREASURY DEPARTMENT

Washington

February 12, 1926.

IT:CA:2332-4-60D

Bankers Pocahontas Coal Company,
Welch, West Virginia.

Sirs:

The determination of your income and profits tax liablity for the years 1921, 1922 and 1923, has been reconsidered in connection with an examination of the books of account and records for 1921 and with the returns filed for 1922 and 1923, and a conference held in the Unit January 4, 1926, and a deficiency in the amount of $16,134.55, has been disclosed, as shown in the attached statement.

In accordance with the provisions of Section 274 of the Revenue Act of 1924, you are allowed 60 days from the date of mailing of this letter within which to file an appeal contesting in whole or in part the correctness of this determination. Any such appeal must be addressed to the United States Board of Tax Appeals, Washington, D. C., and must be mailed in time to reach that Board within the 60-day period.

Where a taxpayer has been given on opportunity to appeal to the Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has appealed and an assessment in accordance with the final decision on such appeal has been made, no claim in abatement in respect of any part of the deficiency will be entertained.

If you acquiesce in this determination and do not desire to file an appeal, you are requested to sign the inclosed agreement consenting to the assessment of the deficiency and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT: CA:2332-4-60D. In the event that you acquiesce in a part of the determination, the agreement should be executed with respect to the items agreed to.

Respectfully,

D. H. BLAIR
Commissioner
By C. R. NASH
Assistant to the Commissioner.

Inclosures:
Statements
Agreement—Form A
Form 882.

(28) STATEMENT

February 12, 1926.

IT:CA:2332-4-60D

In re: Bankers Pocahontas Coal Company, Welch, West Virginia.

	Deficiency in Tax
1921	$7,871.64
1922	4,149.24
1923	4,113.67
Total	$16,134.55

1921

ADJUSTMENTS TO INCOME

Net income reported on return		$8,989.53
Additions:		
1. Depletion return	$50,000.00	
Depletion, revenue agent's report	11,966.69	$38,033.31
Corrected net income		47,022.84

EXPLANATION OF ADJUSTMENT TO NET INCOME

1. See Explanation #3, Adjustments to Net Income for 1920.

INVESTED CAPITAL

Capital Stock, revenue agent's report	$150,000.00
Surplus, revenue agent's report	24,443.65
(1) Undervaluation of coal lands	132,586.41
Total	**$307,030.06**

Deductions:

(2) Preceding year's tax, 1920 $7,586.84 prorated	$3,206.20	
(3) Dividends	9,000.00	
(4) Dividends	13,170.90	25,377.10
Invested capital		$281,652.96

EXPLANATION OF ADJUSTMENTS TO INVESTED CAPITAL (29)

(1) See Explanation (1) of Adjustments to Invested Capital for 1920.

(2) See Explanation (2) of Adjustments to Invested Capital for 1920.

(3) See Explanation (3) of Adjustments to Invested Capital for 1920.

(4) Dividends paid after the expiration of the first sixty days in the taxable year will be deemed to be paid out of the net income available for such purpose on the date when it is payable, in accordance with Articles 857 and 858, Regulations 62.

DEDUCTIONS FOR DIVIDENDS

Available earnings for year		$47,022.84
Tentative tax for year		8,251.34
Amount available for dividends		$38,771.50
Dividends paid April 18		22,500.00
Earnings for 17 days	$1,805.74	
Plus	2,059.80	3,865.54
Paid from surplus		$18,634.46
Prorated for 258 days		13,170.90

COMPUTATION OF TAX

Invested Capital		$281,652.96
Excess profits credit		25,532.24
Excess profits tax		4,298.12
Profits tax		$ 4,298.12
Net income	$47,022.84	
Less:		
Profits tax	4,298.12	
Balance subject to 10% tax	$42,724.72	
Amount of tax at 10%		4,272.47
Total tax assessable		$8,570.59
Original tax		698.95
Deficiency		$7,871.64

(30) 1922

ADJUSTMENTS TO INCOME

Net income reported		$28,753.21
Additions:		
1. Depletion, return	$50,000.00	
Depletion allowable	16,806.09	33,193.91
Corrected net income		$61,974.12

EXPLANATION OF ADJUSTMENT TO NET INCOME

1. Depletion has been allowed in accordance with the data on file in this office.

COMPUTATION OF TAX

Net income	$61,947.12	
Balance subject to tax at 12½%	61,947.12	
Amount of tax at 12½%		$7,743.39
Total tax assessable		7,743.39
Original tax		3,594.15
Deficiency		$4,149.24

1923

ADJUSTMENTS TO INCOME

Net income reported on return		$25,747.11
Additions:		
1. Depletion, return	$50,000.00	
Depletion allowable	17,090.60	$32,909.40
Corrected net income		$58,656.51

EXPLANATION OF ADJUSTMENTS TO NET INCOME

1. See Explanation (1), Adjustments to Net Income for 1922.

(31) COMPUTATION OF TAX

Net income	$58,656.51	
Balance taxable at 12½%	58,656.51	
Amount of tax at 12½%	7,332.06	
Total tax assessable		$7,332.06
Original tax		3,218.39
Deficiency		$4,113.67

You are advised that the additional information submitted under date of January 22, 1926, has been given consideration in the adjustments as shown herein.

(32) **STATEMENT**

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

v. Docket No. 42664.

Commissioner of Internal Revenue,
Respondent.

The petition, amended petition and answer herein are identical in substance with same in Appeal 14517, as affecting adjustments and deficiencies herein contested for the calendar years 1924, 1925 and 1926, and same are therefore here omitted, excepting Paragraph (h) thereof and the deficiency letter here appearing:

(h) That its return of income for the several years has been made upon a cash receipt and disbursement basis, including in each year the income attributable to same; that its payments under said written instruments are due each month, but do not come to hand until the subsequent month or months; that petitioner included in (33) its 1919 return of income payments due in 1919, but not actually shown upon its books until January and February, 1920, in the amount of $5,434.66 and an income tax refund of $180.00, which was likewise not entered on its books until January, 1920; that the adjustment proposed in the deficiency letters of February 12, 1926, and February 15, 1926, including said items in 1920 income, is contrary to established accounting methods of petitioner and causes petitioner to report same a second time as taxable income.

(34) COPY

Docket No. 42664
NP-2
MAILED
Jan. 15, 1929

IT:AR:C
JHP-60D

Bankers Pocahontas Coal Company,
Welch, West Virginia.

Sirs:

In accordance with Section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the years 1924, 1925 and 1926 discloses a deficiency of $16,919.88, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter for a redetermination of your tax liability.

HOWEVER, IF YOU DO NOT DESIRE TO PETITION, you are requested to execute the enclosed Form 866 and forward both original and duplicate to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement form will expedite the closing of your return by permitting an early assessment of any deficiencies and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assessment is made, whichever is earlier; WHEREAS IF NO AGREEMENT IS FILED, interest will accumulate to the date of assessment of the deficiencies.

Respectfully,

D. H. BLAIR,
Commissioner.
By (Signed) C. B. ALLEN,
Deputy Commissioner.

Enclosures:
Statement
Form 866
Form 882
Schedules 1 to 6, inclusive
eco-3

IT:AR:C
JHP-60D

STATEMENT OF RETURNS EXAMINED

(35) AND

RESULTING TAX LIABILITY

Company	Year	Form	Date Filed
Bankers Pocahontas Coal Company	1924	1120	March 14, 1925
	1925	1120	Tentative March 15, 1926 Final May 15, 1926
	1926	1120	Tentative March 15, 1927 Final May 12, 1927

TAX LIABILITY

Company	Year	Deficiency
Bankers Pocahontas Coal Company	1924	$3,362.17
	1925	6,419.04
	1926	7,138.67
Total		$16,919.88

This audit is based upon Revenue Agent's report for the years 1924, 1925 and 1926 which upon review has been approved by this office except as to adjustments for allowable depletion.

Careful consideration has been given to the contention set forth in your protest, sworn to December 10, 1927, filed with the Internal Revenue Agent in Charge, Huntington, West Virginia, and to the additional information submitted in your brief dated November 9, 1928 and at a conference held in Washington, D. C., on December 12, 1928.

It is held by this office that, for income tax purposes, the damages in the amount of $3,770.40 received from the Flanagan Coal Company in 1924 have the status of royalties received, accordingly depletion has been allowed on the 15,000 tons estimated to have been damaged.

No adjustment is deemed to be necessary in regard to curtailment of notes receivable due from Welch Armature Company since such amount was not included in your taxable income.

Inasmuch as dividends were not deducted from gross income no adjustment is necessary for this item.

Your total tax liability for the years involved amounts to $20,478.05 as shown on the attached Agreement Form 866.

eco-3

(36) Bankers Pocahontas Coal Company Year ended December 31, 1924.

Schedule 1

Net Income

Net income as disclosed by return		$28,465.36
As corrected		55,362.70
Net adjustment		$26,897.34
Unallowable deductions and additional income:		
(a) Excessive depletion	$26,926.07	
Total		26,926.07
Nontaxable income and additional deductions:		
(b) Additional miscellaneous expense	$ 25.96	
(c) Nontaxable interest on Liberty Bonds	2.77	
Total		28.73
Net adjustment as above		$26,897.34

Schedule 1-A

Explanation of Items Changed

(a) Based on the terms of the leases in effect on March 1, 1913, the recoverable tonnages and productions, the following computations of values are in conformity with the regulations and are used instead of the $.036 originally allowed.

eco-3

Bankers Pocahontas Coal Company Year ended
(37) December 31, 1924.

Schedule 1-a (Continued.)

Explanation of Items Changed (Continued)

Depletion Schedule—Year ended December 31, 1924.

Companies from which royalties were received.	Production	Rate	Depletion Allowed
Fall River Pocahontas Coal Company*	15,000	.0255	$ 382.50
	94,296	.0255	2,404.55
Superior Pocahontas Coal Company	120,000	.0298	3,576.00
Monarch Smokeless Coal Company**	162,452	.0208	3,379.00
Kingston Pocahontas Coal Company (Oregon and Exeter leases)	444,125	.0298	13,234.92
Fordson Coal Company	16,981	.00571	96.96
Total			$23,073.93
Depletion claimed			50,000.00
Excessive depletion			$26,926.07

*Coal mined by Flanagan Coal Company from this lease.

**Includes production of New Pocahontas Coal Company.

(b) and (c) Self explanatory.

Schedule 2.

Computation of Tax

Net income for taxable year	$55,362.70
Income tax 12½%	6,920.34
Tax previously assessed	$3,558.17
Additional tax to be assessed	$3,362.17

eco-3

(38) Bankers Pocahontas Coal Company Year ended December 31, 1925.

Schedule 3

Net Income

Net loss as disclosed by return		($3,467.07)
As corrected		49,377.26
Net adjustment		$52,844.33
Unallowable deductions and additional income:		
(a) Haulage over right of way	$ 30.29	
(b) Royalties received	75,250.32	
(c) Taxes collected from lessees	14,031.61	
(d) Rent and office expense	198.10	
(e) Depreciation	14.27	
(f) Printing and stationery	257.10	
Total		$89,781.69
Nontaxable income and dditional deductions:		
(g) Taxes	$13,931.59	
(h) Rents	350.81	
(i) Traveling expenses	444.11	
(j) General expense	5.20	
(k) Depletion	22,205.65	
Total		$36,937.36
Net adjustment as above		$52,844.33

Schedule 3-A

Explanation of Items Changed

(a), (d), (e), (f), (h), (i) and (j) income and expense adjustments have been made to bring the return in agreement with amounts disclosed by books.

(b) The Bureau holds that the royalties received constitute gross income and that such action is in accord with Treasury Decision 3562.

(c) and (g) Taxes paid for your company by the leases is deemed to be income to your company. However, such taxes have been allowed as deductions from your gross income.

(k) See explanation A—Schedule 1-A.

eco-3

(39) Bankers Pocahontas Coal Company Year ended December 31, 1925.

Schedule 3-a (Continued)

Explanation of Items Changed.

(k) Depletion Schedule—Year ended December 31, 1925.

Companies from which royalties were received	Production	Rate	Depletion Allowed
Fall River Pocahontas Coal Company	84,141	.0255	$2,145.59
Superior Pocahontas Coal Company	120,000	.0298	3,576.00
Monarch Smokeless Coal Company	147,184	.0208	3,061.43
Kingston Pocahontas Coal Company (Oregon and Exeter Leases)	447,444	.0298	13,333.83
Fordson Coal Company	15,551	.00571	88.80
Total			$22,205.65

Schedule 4

Computation of Tax

Net income for taxable year	$49,377.26
Income tax 13 per cent	$ 6,419.04
Tax previously assessed	None
Tax to be assessed	$ 6,419.04

eco-3

Bankers Pocahontas Coal Company Year ended
(40) December 31, 1926.

Schedule 5

Net Income

Net income as disclosed by return		($3,476.41)
As corrected		52,879.06
Net adjustment		$56,355.47
Unallowable deductions and additional income:		
(a) Haulage over right of way	$ 233.42	
(b) Royalties received	79,761.09	
(c) Water Rent—McClaren and Summers	27.00	
(d) Rent—Appalachian Power Company	350.81	
(e) Taxes collected from lessees	13,779.03	
(f) Depreciation	14.27	
(g) General Expense	147.60	
Total		$94,313.22
Nontaxable income and additional deductions:		
(h) Rent and office expense	$ 24.60	
(i) Taxes	13,939.82	
(j) Depletion	23,993.33	
Total		$37,957.75
Net adjustment as above		$56,355.47

eco-3

Bankers Pocahontas Coal Company Year ended
(41) December 31, 1926.

Schedule 5-a

Explanation of Items Changed

(a), (c), (d), (f), (g) and (h) Income and expense accounts have been adjusted to agree with amounts disclosed by books.

(b) See explanation (b) Schedule 3-a.

(e) and (i) See explanation (c) and (g) Schedule 3-a.

(j) See explanation (a) Schedule 1-a.

Depreciation Schedule. Year ended Dec. 31, 1926.

Companies from which royalties were received	Production	Rate	Depletion Allowed
Fall River Pocahontas Coal Company	88,073	.0255	$2,245.86
Superior Pocahontas Coal Company	120,000	.0298	3,576.00
Monarch Smokeless Coal Company	167,030	.0208	3,474.22
Kingston Pocahontas Coal Company (Oregon and Exeter Leases)	483,529	.0298	14,409.16
Fordson Coal Company	50,453	.00571	288.09
Total			$23,993.33

Schedule 6

Computation of Tax

Income Tax

Net income for taxable year	$52,879.06
Income tax 13½%	7,138.67
Total previously assessed	None
Tax to be assessed	$ 7,138.67

MOTION FOR CONSOLIDATION

(42) Filed Apr. 27, 1929.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket No. 42664.

Commissioner of Internal Revenue,
Respondent.

Petitioner, by counsel, moves the Board:

1. To advance and consolidate this appeal for hearing with appeals of petitioner Nos. 14516 and 14517 now set for hearing on Thursday, May 2, 1929,

For cause:

That same presents the same issues as the earlier appeals.

That respondent, (Mr. McDowell) has no objection.

(Signed) CAMDEN R. McATEE,
Counsel for Petitioner.

GRANTED
APRIL 30, 1929
(Sgd.) B. H. Littleton
Member,
U. S. BOARD OF TAX APPEALS

FINDINGS OF FACT AND OPINION.

(43) 18 B. T. A. ---------.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Co.,
Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 10472, 14516, 14517, 25275, 32170, 42664. Promulgated January 22, 1930.

Royalties received under leases of coal lands are held to constitute gross income and not proceeds from the sale of coal in place.

Money received in compromise of a suit to recover the value of coal extracted by a trespasser, plus damages to the property held, on the record, to constitute taxable income.

Proper depletion rate per ton of coal mined determined.

Camden R. McAtee, Esq., and Wells Goodykoontz, Esq., for the petitioners. M. E. McDowell, Esq., and Frank B. Schlosser, Esq., for the respondent.

These proceedings, consolidated for hearing and de-
(44) cision, involve deficiencies as follows:

Docket No.		
14517	1920	$6,797.56
14516	1921	7,871.64
	1922	4,149.24
	1923	4,113.67
42664	1924	3,362.17
	1925	6,419.04
	1926	7,138.67
10472	1919	863.62
	1920	1,181.02
	1921	1,123.48
25275	1922	2,549.05
	1923	1,817.77
32170	1924	95.09
	1925	1,144.47

In the petitions of Bankers Pocahontas Coal Co. (Docket Nos. 14517, 14516, and 42664), the first contention made is that there is no tax due, upon the ground that the amounts received by the petitioner during the taxable years represented installment payments upon the sales of coal in place, which coal had been sold prior to March 1, 1913.

The second contention is that if the Bankers Pocahontas Coal Co. is to be considered as a lessor, then the amount of depletion which has been allowed to that company has been erroneously computed by the respondent.

For the year 1920, there are two incidental questions which simply amount to the inclusion in 1920 of income which was previously reported for 1919. For 1924, there is an incidental question arising by reason of damages received by the petitioner, the contention being that the (45) amount received as damages to property is not properly includable in gross income.

The contentions in the petitions of D. J. F. Strother (Docket Nos. 10472, 25275, and 32170) are:

(1) That the petitioner received no taxable income when he received distributions from Bankers Pocahontas Coal Co., claimed by the petitioner to be tax-exempt by

reason of being distributions of a part of the capital of that company;

(2) That the depreciation rate properly allowable to the Bankers Pocahontas Coal Co., if not properly allowed, has distorted his income;

(3) That the Bankers Pocahontas Coal Co., has made distribution each year of all of its revenues derived from its contracts; that it has accordingly distributed its depletion reserve and that the petitioner should be entitled to an allowance for that depletion reserve in the computation of dividends received from it.

FINDINGS OF FACT

In July, 1912, the Bankers Pocahontas Coal Co., a West Virginia corporation (hereinafter sometimes called the corporation), acquired the fee simple title to approximately 6,200 acres of coal lands, including both the surface and the mineral rights in the State of West Virginia. The land had no appreciable value except for the coal (46) content.

Upon incorporation in 1912, the corporation acquired by formal assignment and has continued to retain the beneficial interest of the original owners in certain contracts affecting the coal content which were executed in 1901 and 1902 with various operating companies and to which contracts the 6,200 acres and coal content were subject.

These contracts were originally prepared by D. J. F. Strother, who at that time was attorney, director, and stockholder in the predecessor corporations. The form of the contracts is that prevailing in the West Virginia coal fields, which followed the Pennsylvania form of contracts as introduced by Pennsylvanians who were largely instrumental in the early coal development in the West Virginia field.

By agreement of parties a copy of such contracts was offered and received in evidence as typical of the several

contracts existing on the acreage acquired by the corporation in 1912. The specimen contract provides in part as follows:

This contract of lease, made this 17th day of June, 1901, between the Tug River Coal Land Company, a corporation, authorized and doing business under and by virtue of the laws of the State of West Virginia, party of the first part, hereinafter called the Lessor, and the Cletus Coal and Coke Company, a like corporation, hereinafter called the Lessees.

Witnesseth: First: That in consideration of the terms, conditions and stipulations hereinafter set forth to be performed and observed by the lessees, the Lessor doth demise, let and lease for coal mining and coal cokeing purposes only, to the lessee, for the period of thirty (30) years, from the 1st day of January, 1901, a certain tract of land situate, lying and being in the County of McDowell and State of West Virginia, on the waters of Tug River containing eight hundred acres, more or less (47) and bounded and described as follows: (Description omitted.)

The Lessor covenants to and with the said Lessee that it has good right and title to said land, and that the said Lessee shall have quiet, and peaceable enjoyment of the same during the continuance of this lease.

SECOND: The Lessees shall have the sole and exclusive privilege of mining and coking coal on the above described premises and of conducting a general mercantile business thereon during the continuance of this lease, and the privilege of using so much of the surface of said land and so much of the timber, stone, sand, clay and water as may be necessary for the mining, coking and building purposes of said Lessees, but for no other purpose.

* * * * * * *

THIRD: In consideration thereof, the Lessees hereby covenant and agree to pay to the Lessor, its successors and assigns, during the continuance of this lease, as rental for the said premises, the following royalties, to-wit:

Ten (10) cents per ton for each and every ton of 2240 pounds of coal mined, dug, carried away from or sold or used on the said premises for any other purpose than the manufacture of coke; and fifteen (15) cents for each and every ton of 2240 pounds of coke manufactured upon the said premises, and sold thereon or therefrom. * * *

* * * * * * * *

SEVENTH: The Lessees agree and bind themselves to pay to the Lessors the sum of three thousand dollars for the first year, dating from the 1st day of November, 1901, and the sum of five thousand dollars for each and every year thereafter, during the continuance of this lease, as a minimum rental or royalty for the property herein demised, whether the quantity of coal mined and coke manufactured shall produce that amount of royalty or not, but the Lessees shall have the privilege of mining the next succeeding year, free of royalty, a sufficient amount of coal above the amount necessary to produce the minimum royalty for that year to reimburse themselves for the deficiency in the preceding year. * * *

* * * * * * * *

NINTH: The Lessees agree to pay all the taxes that (48) may be assessed against the demised property and the improvements thereon, or upon the coal mined or coke manufactured, during the continuance of this lease, all other assessments by operation of law whatsoever, when and as the same may become due.

* * * * * * * *

ELEVENTH: At the termination of this lease, otherwise than by forfeiture, all the improvements placed upon the said surface of the demised premises, by the Lessees, shall be valued by two disinterested persons, one to be chosen by each of the parties hereto, and in case of their disagreement, these two shall choose a third, and the persons thus chosen shall value said improvements, and the Lessor shall have the privilege of purchasing said improvements at such valuation, within thirty (30) days after notice thereof. If the Lessor shall not, within said thirty days, accept said improvements, at such valuation, the Lessees shall have the privilege

of removing the same from the leased premises within the period of ninety days from the expiration of said thirty days.

TWELFTH: The Lessees shall have the right to at the expiration of the said thirty years, renew this lease, with the terms, stipulations and agreements as herein set forth, provided that they shall have complied with and performed all the conditions, covenants, agreements and stipulations to be by them complied with or performed.

THIRTEENTH: It is hereby mutually understood and agreed that the covenants, agreements, stipulations herein contained to be performed by the one party or the other, shall be binding on the parties hereto, their successors and assigns.

IN WITNESS WHEREOF, the parties hereto have caused these presents to be signed in their corporate names by their respective presidents, and their corporate seals to be hereunto affixed as of the day and year first above written.

All of these agreements were in the main, with the exception as to minor and non-essential provisions, the (49) same as the sample agreement set forth above as the Cletus lease.

From time to time these agreements were reassigned by the lessees to new and different operating lessees, largely with the permission of the lessor corporation.

The cost to the corporation of the properties acquired by it was between $407,000 and $507,000.

The contracts on the property on March 1, 1913, are shown by the following:

SCHEDULE 1

CONTRACTS ON MARCH 1, 1913.

Lessee at 3/1/13	Approximate Acreage	Royalty per ton	Minimum Royalty per annum
Lease #1 Vaughan Coal & Coke Co.	1000	8c	$5,000
#2 Superior Pocahontas Coal Co.	1200	10c	5,000
#3 New Pocahontas Coal Co.	1300	7c	4,000
#4 Oregon Coal & Coke Co.	2000	10c	10,000
#5 Pocahontas Smokeless Coal Co.	600	5c	None
#6 J. B. B. Coal Co.	100	1c(haulage)	300

The estimated recoverable tonnage on March 1, 1913,
(50) is shown by the following:

SCHEDULE 2

ESTIMATED RECOVERABLE TONNAGE ON MARCH 1, 1913

Lease #1 Vaughan Coal & Coke Co.	2,416,452	
Lease #2 Superior Pocahontas Coal Co.	2,309,444	
Lease #3 New Pocahontas Coal & Coke Co.	3,773,835	
Lease #4 Oregon Coal & Coke Co.	4,906,902	upper or Welch Seam
	22,765,666	lower seam
Lease #5 Pocahontas Smokeless Coal Co.	493,172	
Lease #6 J. B. B. Coal Co.	943,171	
Total	37,608,642	

The tonnage mined and royalty receipts of the corporation for the years 1913 to 1919, inclusive, is shown by leases as follows:

	Tonnage mined	Royalty Receipts
Lease No. 1	393,379	34,497.20
Lease No. 2	528,255	61,263.41
Lease No. 3	571,502	52,352.49
Lease No. 4	472,980	77,465.45
Lease No. 5	250,601	11,874.92
Lease No. 6	664,991	6,641.15
Total	2,881,708	244,094.62

The tonnage mined, the tonnage paid for, and the royalty receipts for the taxable years involved in these pro-
(51) ceedings are shown by the following:

Lease No. 1—Fall River Pocahontas Collieries Co.

Year	Tonnage mined	Paid for	Receipts
1920	71,594	71,593	5,727.48
1921	98,587	98,587	7,886.98
1922	85,132	85,132	6,810.55
1923	81,373	81,373	6,509.88
1924	95,859	85,859	7,668.72
1925	81,552	81,557	6,524.16
1926	90,764	90,765	7,261.12

Lease No. 2—Superior Pocahontas Coal Co.—Cletus Mine

Year	Tonnage mined	Paid for	Receipts
1920	57,189	120,000	12,000
1921	54,660	120,000	12,000
1922	55,864	120,000	12,000
1923	51,422	120,000	12,000
1924	57,928	120,000	12,000
1925	68,804	120,000	12,000
1926	90,029	120,000	12,000

Lease No. 3—W. E. Deegans (Later New Pocahontas Coal Co. and Monarch Smokeless Coal Co.)

Year	Tonnage mined	Paid for	Royalty rate	Receipts
1920	113,086	113,686	.07	8,372.78
1921	92,983	104,695	.07	7,916.02
1922	141,895	141,895	.07	7,328.66
1923	131,961	131,961	.08	10,556.83
1924	160,428	160,440	.08	12,835.26
1925	151,694	151,619	.08	12,135.57
1926	166,280	164,533	.08	13,162.70

Lease No. 4—Oregon Coal Company (Later Solvay Collieries Company and Kingston Pocahontas Coal
(52) Company).

WARWICK MINE

Year	Tonnage mined	Paid for	Receipts
1920	86,918	100,000	10,000.00
1921	15,297	100,000	10,000.00
1922	109,853	100,002	10,000.02
1923	113,565	113,659	11,365.72
1924	125,811	125,811	12,581.10
1925	91,170	100,000	10,000.00
1926	118,273	118,827	11,827.70

Lease No. 4—Solvay Collieries Company (Later Kingston Pocahontas Coal Co.)

EXETER MINE

Year	Tonnage mined	Paid for	Receipts
1920	19,231	187,500	18,750.00
1921	25,024	306,250	30,625.00
1922	45,483	370,433	37,043.38
1923	74,152	340,782	34,078.20
1924	103,877	343,657	34,365.70
1925	117,792	325,000	32,500.00
1926	153,717	335,115	33,511.56

Lease No. 5—Pocahontas Smokeless Coal Company (Later Central Pocahontas Coal Company.)

Year	Tonnage mined	Paid for	Receipts
1920	27,671	25,758	1,287.88
1921	5,622	4,111	205.57
1922	8,611	8,773	438.65
1923 (Jan.1-Mch.31)	3,877	3,877	193.85

(53) Lease No. 6—Hensley Coal Company (Later known successively as J. B. B. Coal Company, Dexear Pocahontas Coal Company and Fordson Coal Co.) The payment of 1c per ton ($300.00) minimum per year, is a haulage fee for use of an easement over Bankers Pocahontas property to coal mined on other properties by the operators.

Year	Tonnage mined	Paid for	Receipts
1920	80,506	80,506	805.06
1921	38,990	6,827	68.27
1922	19,811	-----	-----
1923	20,811	15,771	157.71
1924	12,025	12,025	120.25
1925	12,640	12,640	126.40
1926	7,258	51,822	518.22

In the several taxable years in controversy the corporation was upon a cash receipts and disbursements basis of accounting and its income, except minor items not in controversy, consisted of payments received under the several contracts from the various operating companies, and income and profits-tax returns were filed for each of the taxable years and thereafter audited by the Commissioner resulting in the deficiency notice forming the basis of the present proceedings.

In computing the deficiencies the Commissioner considered the relation of the corporation and the operating companies to be that of lessor and lessee and allowed the corporation a depletion deduction of $0.036 per ton

mined for the years 1920 to 1926, inclusive, the same depletion rate as was allowed by the Commissioner for 1919 and prior years.

For prior years 1914 to 1919, inclusive, the Commissioner proposed additional taxes in the amount of $6,267.08 and required the corporation to pay same, which (54) thereafter brought an action on February 17, 1923, in the United States Court for the Southern District of West Virginia against the collector to recover same on the grounds that payments under said contracts received by the corporation were the proceeds of a sale of coal in place consummated before March 1, 1913, or of choses in action existing on said date, or that petitioner plaintiff, as a lessor, was entitled to a unit depletion rate of not less than $0.05 per ton mined in the computation of net taxable income, and consequently said taxes were erroneously and illegally assessed and collected. The issues were made in said action, and same were submitted for judgment upon the evidence adduced by the parties, and were decided by opinion of the court and judgment entered thereon that petitioner plaintiff in the computation of said taxes was entitled to a depletion unit of $0.05 per ton instead of $0.036 computed by the Commissioner. A recovery of $5,373.01 from said collector by petitioner plaintiff was adjudged and said judgment was duly paid by the United States. In said action the Bankers Pocahontas Coal Co., one of the petitioners herein, was plaintiff; plaintiff petitioner appearing in its own right and the collector as defendant, who was defended in said action by the United States District Attorney and the Solicitor of Internal Revenue (now General Counsel). In this proceeding and in said court action the subject matter of the action and of these proceedings is the same, namely, the depletion unit allowable in computing the amount of such depletion deduction as will return to the taxpayer the capital value existing in the coal content of the corpora(55) tion's property as of March 1, 1913.

In his computation of invested capital of the corporation for the calendar year 1920 in the deficiency appealed from herein, the Commissioner used the tax computation determined in said action as due and owing for the calendar year 1919, which was based upon the allowance of a

$0.05 depletion rate for 1919. In the years subsequent to 1919, the Commissioner has applied the depletion rate of $0.036 per ton. The court action was instituted February 17, 1923, and the judgment therein was entered January 31, 1928. The deficiency letters were mailed for 1920 on February 15, 1926; for 1921, 1922, and 1923 on February 12, 1926; for 1924, 1925, and 1926 on January 15, 1929. Before the issue of the last named deficiency notice the attention of the Commissioner was specifically called to the pendency and decision of the court action.

In the several taxable years, and particularly in 1919, the corporation received its contract payments each month and same when received were about thirty days overdue. The payment for December was consistently reported in the year's receipts, although same did not come to hand until January. In December, 1919, the corporation received a tax refund of $180, which it put on its books in January, 1920, and likewise received a contract payment of $5,434.66. These amounts were reported as income for 1919 and the Commissioner has included same again as 1920 income, as shown by the books to have been received in the latter year.

In 1920, the Flanagan Coal Co., which owned land ad- (56) jacent to the petitioner corporation, trespassed on the land of the petitioner corporation and removed coal to which it had no right. It then destroyed the entries so that the damage or extent of the operation could not be determined. The corporation discovered the situation in 1923 and brought suit for damages and, as a result of a compromise of the suit, received in 1924, $3,-770.40 in settlement and adjustment of the controversy. The petitioner corporation had no contractual relation with the trespasser and the settlement had no relation to the coal extracted, as the amount of same could not be determined. The Commissioner held the damages received were equivalent to a royalty and adjusted same by the allowance of $0.036 per ton as depletion on 15,000 tons estimated to have been damaged or removed by the trespasser.

In the several years involved herein the petitioner, Strother, as one of the corporation's stockholders, re-

ceived payments from the Bankers Pocahontas Coal Co. and reported same in his returns but did not return them as taxable income. The corporation received said amounts from its operating contracts and entirely distributed them, including any depletion reserve. No allowance was made by the Commissioner to the petitioner, Strother, for any depletion reserve received by him and the Commissioner added the entire receipts to his net income and has determined deficiencies accordingly.

OPINION

Smith: In these proceedings the Bankers Pocahontas (57) Coal Co. contends that it received no income during the taxable years and all of the moneys received as royalties were in part payment of coal in place which had been sold prior to March 1, 1913; that the typical contract quoted in part in the findings of fact constituted a sale of coal in place made before March 1, 1913, under the laws of West Virginia, and that on March 1, 1913, the petitioner held only a chose in action from which no taxable income was subsequently received; that leasing agreements similar to those involved in these proceedings have been held by the courts of Pennsylvania in Delaware & Hudson Canal Co. v. Hughes, 183 Pa. 66; 38 L. R. A. 826; Lehigh & Wilkesbarre Coal Co. v. Wright, 177 Pa. 387, 35 Atl. 919; Denniston v. Haddock, 200 Pa. 426, 50 Atl. 197; and by the courts of West Virginia in Wallace v. Elm Grove Coal Co., 58 W. Va. 449, 52 S. E. 485; National Coal Co. v. Overholt, 94 S. E. 735 (W. Va.); to constitute sales of coal in place; that the Board is bound to give the same effect to such leasing agreements as has been given to them by the courts of the States of Pennsylvania and West Virginia.

This is the same contention as has been made before the Board in many different cases. Beginning with the case of Nelson Land & Coal Co., 3 B. T. A. 315, and following down through a number of decisions, this Board (58) has uniformly held that sums received as bonus or royalties from leases of oil and mineral rights were not income from the sale or exchange of capital assets, but constituted a part of the gross income that the peti-

tioner was obligated to return as a part of its gross income. It is likewise the same contention which was made before the District Court of the United States for the Southern District of West Virginia in the case of Bankers Pocahontas Coal Co. v. Albert B. White, referred to in our findings, which was a suit for the recovery of additional taxes paid for the years 1914 to 1919. The learned judge of that court disposed of that case in the following language:

This brings on the first contention of the plaintiff, that is, that the plaintiff, by the reserved rentals and royalties, is being paid for the land and the coal thereunder, and that such rentals and royalties are not "income" but "purchase money."

Personally, I believe this statement to be true, but I cannot, in the face of all the decisions, sustain it here.

I therefore hold, that the royalty payments are income, and should pay a tax as such.

Judicial decisions upon the point are many. See Hirschi v. United States, Ct. Cl. , decided May 6, 1929; Berg v. Commissioner, 33 Fed. (2d) 641, certiorari denied 50 S. Ct. 69; Stanton v. Baltic Mining Co., 240 U. S. 103; Von Baumbach v. Sargent Land Co., 242 U. S. 503; United States v. Biwabik Mining Co., 247 U. S. 116. In Hirschi v. United States, supra, the court stated:

The one question involved is whether the income re-
(59) ceived by the plaintiff from said lease is taxable as income from the sale of capital assets or his ordinary income. If it is from the sale of capital assets the plaintiff is entitled to a refund; if it is not, he is not so entitled. Since the decision in Stratton's Independence v. Howbert, 231 U. S. 399, following through Stanton v. Baltic Mining Co., 240 U. S. 103; Von Baumbach v. Sargent Land Co., 242 U. S. 503; United States v. Biwabik Mining Co., 247 U. S. 116, it has been consistently held that the trustees received from such leases of oil and mineral lands were to be treated as gross income. The principle is too well established to require extended discussion.

* * * * * * * * * *

The Federal Government is not limited in its selection of subjects for taxation by the construction of the State courts as to the property rights of individuals, provided the subject taxed was primarily a proper subject for taxation. Congress in passing a revenue act does not, and is not called upon to suit the revenue system of the country to the varying and conflicting decisions and laws of the different states. A revenue act is an act of Congress passed in the exercise of its constitutional right, and therefore the supreme law of the land, and where the constitutional powers of the Federal Government and the States conflict those of the States must give way.

Petition for writ of certiorari was denied by the Supreme Court in this case on October 21, 1929.

In Van Devender, 8 B. T. A. 697, contracts in West Virginia made by the petitioner and others from the mining of coal were held to constitute leasing agreements upon the authority of Henry L. Berg and Wife, 6 B. T. A. 1287, and Rosenberger v. McCaughn, 20 Fed. (2d) 139. Counsel for the petitioners suggest, however, that in the Van Devender case the petitioner made the contracts and (60) that they were not transferred to third parties; that the instant proceedings present the case of such transfer and that if there is any income received from the contract subject to tax it is ascertained by the exclusion of all capital from same, according to the final decision of Rosenberger v. McCaughn, 25 Fed. (2d) 699. We see no justification for the distinction sought to be made. The Bankers Pocahontas Coal Co. received its property in July, 1912, subject to certain leases upon the property. In our opinion the corporation simply stands in the shoes of the original lessors. The royalties received by it constitute part of its gross income. From such income it is entitled to deduct a reasonable amount for the depletion of its property during the taxable years.

In computing the deficiencies for the years 1920 to 1926, the respondent has used a depletion rate of $0.036 per ton of ore mined each year. The respondent held

that this was a reasonable depletion rate and that such rate multiplied by the tons mined each year constituted a reasonable deduction for depletion. The corporation taxpayer contends that this is not a proper rate and that its application does not permit the deduction of a reasonable amount for depletion. In support of its contention it submits the decision of the District Court made in the above cited case of Bankers Pocahontas Coal Co. v. Albert B. White, in which the court found that a reasonable depletion rate was five cents per ton multiplied by the number of tons of ore mined during each taxable (61) year. The evidence before the District Court was introduced before the Board and in addition much additional evidence showing the cost of the properties to the Bankers Pocahontas Coal Co. at the time they were acquired in 1912, and likewise the agreed estimated tonnages in each of the leases upon the land. With respect to the cost of the properties to the petitioner corporation D. J. F. Strother, the president of the corporation, testified as follows:

My recollection is that a bond issue outstanding on the property at that time was either two hundred and forty, or two hundred and sixty thousand dollars; I know I am right in either one amount or the other; we paid out sixty thousand dollars in cash; there were some troubles with the title and we paid on that, at one time, considering this stock at par, $35,000, and we withheld to straighten these titles out, to the Standard Pocahontas Coal Company, 600 acres of coal, which we valued anywhere from $50,000 to $150,000; we settled two or three other claims, and I do not think I am quite now qualified to speak about, of, I think I have them in my file there, some two thousand dollars more.

This would indicate a cost to the petitioner corporation of from $407,000 to $507,000. The evidence as to the March 1, 1913, value of the property is vague. In 1915, an engineer representing the Old Dominion Trust Co. of Richmond, Va., made a report on the company's property in which he stated that there were approximately 20,000,000 tons of mineable coal at an average value of five cents per net ton making a total value of $1,000,000. On or about December 31, 1917, an account was entered

upon the corporation's general ledger debiting coal lands
(62) $1,000,000 with the following explanation:

Estimated value as of March 1, 1913 of 6,000 acres coal land said to contain 20,000 tons of coal at five cents per ton.

The income-tax returns filed for those years claimed a March 1, 1913, value for the property of $1,000,000.

In United States v. Ludey, 274 U. S. 295, it was stated:

* * * The amount of the allowance for depreciation is the sum which should be set aside for the taxable year, in order that, at the end of the useful life of the plant in the business, the aggregate of the sums set aside will (with the salvage value) suffice to provide an amount equal to the original cost. * * *

* * * * * * * * * *

The depletion charge permitted as a deduction from the gross income in determining the taxable income of mines for any year represents the reduction in the mineral contents of the reserves from which the product is taken.

No essential difference is recognized in the decisions of the courts between depreciation and depletion, so far as the nature of the deduction under the taxing acts involved is concerned. Both are designed to return to the taxpayer the cost or March 1, 1913, value of property depreciated or depleted, whichever is the basis for the computation.

The evidence in the instant proceedings is that there was an estimated quantity of coal in place on March 1, 1913, of 37,608,642 tons. No contention is made anywhere that the March 1, 1913, value of this coal in place was in excess of $1,000,000. The depletion unit used by the respondent in his computation of $0.036 per ton will,
(63) upon the exhaustion of the coal deposits, return to the petitioner corporation a total of $1,353,911.11. The depletion rate used by the respondent will therefore return to the petitioner corporation an amount in excess

of the greatest claim made by it as to the value of the coal in place at March 1, 1913.

The respondent has determined that a depletion rate of $0.036 per ton is a reasonable rate. The Commissioner's determination of tax liability is prima facie correct. United States v. Rindskopf, 105 U. S. 418; Avery v. Commissioner, 22 Fed. (2d) 6; Brown v. Commissioner, 22 Fed. (2d) 797; Blair v. Roth, 22 Fed. (2d) 932. If the corporation is entitled to a higher rate of depletion than that determined by the respondent the burden is upon the corporation to prove the inadequacy of the depletion rate used by the respondent. We are of the opinion that it has not sustained that burden of proof.

In Docket No. 14517 the Bankers Pocahontas Coal Co. claims that its income for 1920 was overstated by the inclusion therein of royalties in the amount of $5,434.66 and taxes in the amount of $180, which were taxable as income of the year 1919, for which year the amounts were returned as income. The evidence indicates that the books of account show these receipts in 1920. It is contended, however, that the amounts were actually received by the corporation in 1919 and that it was through negligence that the amounts were not deposited in the bank until 1920. The evidence supports such claim. The contentions of the corporation upon this point are there-
(64) fore sustained.

In Docket No. 42664 it is contended that a certain receipt of the corporation in 1924, amounting to $3,770.40, from the Flanagan Coal Co., did not constitute a receipt of income. This amount was received in compromise of a suit brought against that company by the petitioner "to recover the value of the coal that had been extracted, plus damages to the plant." At the hearing of these proceedings petitioner's president was asked to relate "the facts briefly out of which the condition arose which resulted in the receipt of that amount of money [$3,770.40] in 1924 by your company." Petitioner's president testified:

The Flanagan Coal Company owned an adjoining piece of land to our land; we discovered that they had mined

across our boundary line in a particular seam of coal; I took that up with them and they first said they would pay for it. The matter hung on for some months; this was in 1920 when they had gone in there, at which time the price of coal was very high—anywhere from $6.00 to $15.00 a ton. They did not pay, and when I got my engineers to go down to undertake to measure up how much coal they had gotten out, they found out they had shot in the entries and we could not get in at all, so I brought a suit for damages to the property, and we eventually settled it and we got this $3,770 in 1924, for damage to our property, and that seam of coal I figured and figured over with my engineers as at least $10,000 because they had absolutely destroyed the method of going in on that side of the hill.

He further testified on cross-examination:

We claimed our damages very considerably in excess of that [$3,770.40], but the Flanagan Coal Co. at that time was in a pretty precarious condition financially, and we figured every little bit would help, and we got as (65) much as we could.

The respondent determined that the $3,770.40 in question was a part of the petitioner's gross income; that the trespasser had mined 15,000 tons of coal from the corporation's land; and that the petitioner was entitled to deduct from gross income, in its tax return for 1924, $540 for depletion in respect of the coal removed.

The taxing acts permit the deduction from gross income of losses sustained during the taxable year when not compensated for by insurance or otherwise. (Section 234 (a) (4), Revenue Acts of 1918 and 1921.) If there was a loss sustained by the Bankers Pocahontas Coal Co. as a result of the tortious act of the Flanagan Coal Co., it was sustained in 1920, and the amount of the loss not compensated for by insurance or otherwise is deductible from the gross income of 1920. The evidence does not, however, afford facts from which the amount of the loss may be determined. We do not know what the cost of the coal removed by the trespasser was to the petitioner nor its March 1, 1913, value. If the Banker's Pocahontas

Coal Co. is predicting the loss and damage to the property upon the inflated prices of coal in 1920, we think there is no justification for basing a deductible loss upon such inflated values. Joseph E. Hubinger, 13 B. T. A. 960, affirmed by the Circuit Court of Appeals for the Second Circuit December 2, 1929. The deduction of any loss for 1920 must therefore be disallowed for lack of proof of
(66) the amount of the loss, if any.

The same situation obtains with respect to the year 1924. The company received from the trespasser $3,770.40. The petitioner has found that all but $540 of this amount (which he has allowed as a deduction from gross income as depletion) constituted taxable income of the company for 1924. The company has submitted no evidence that the cost or March 1, 1913, value of the coal removed by the trespasser was in excess of $540 or that such basis plus damages to the property was in excess of $540. The determination of the Commissioner is therefore sustained for lack of evidence showing error on the part of the respondent. Joseph E. Hubinger, supra.

In Docket No. 14517, with respect to the year 1920, and in Docket No. 14516, with respect to the year 1921, additional error is alleged in the adjustment of surplus and, therefore, in the computation of the petitioner corporation's invested capital. The correctness of the adjustment depends upon the determination of a proper depletion allowance. It therefore follows that, when a proper depletion rate has been determined under the major issue of the proceedings, the establishment of a proper depletion reserve and, consequently, the proper adjustment of surplus will necessarily follow and be made the subject of appropriate recomputation under the Rule 50 settlement.

With respect to the years 1920 and 1921, the corporation also claims that there has been an improper proration of dividends affecting its invested capital for those years. This raises the question of a tentative tax adjust-
(67) ment such as was involved in L. S. Ayers & Co., 1 B. T. A. 1135. The rule of the Board in L. S. Ayers & Co.,

supra, should be applied in the recomputation of the deficiencies.

The only issues raised in the three proceedings taken by D. J. F. Strother relate to an overstatement of his income for the years in question resulting from the inclusion therein of the dividends received by him from the corporation. The respondent submits that the determination of the nature of the receipt by the corporation under the leases will also determine the nature of the dividends paid out of its receipt to the stockholder. To the extent that the distribution made by the corporation constitutes a distribution of its depletion reserve the amount received by Strother in nontaxable. Parties are in full accord as to the treatment to be given the individual appeals.

Reviewed by the Board.

Judgment will be entered under Rule 50.

MOTION FOR REHEARING AND MODIFIED FINDINGS OF FACT AND OPINION

(68) Filed Feb. 27, 1930.

U. S. BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,

vs. Docket Nos. 14516-17 and 42664.

Commissioner of Internal Revenue, Respondent.

D. J. F. Strother, Petitioner,

vs. Docket Nos. 10472, 25275 and 32170.

Commissioner of Internal Revenue, Respondent.

Come the petitioners herein, and move the Board to set aside its findings of fact and decision promulgated in the above entitled appeals on January 22, 1930, (providing for a Rule 50 redetermination) and to grant petitioners a rehearing, or modified findings of fact and opinion herein, for cause:

1. That the Board erred in including in said findings of fact, statements concerning the contracts upon the property, the estimated recoveries of coal tonnage on March 1, 1913, and the tonnage mined and royalty receipts from each of the several leases; which said evidence was offered at the hearing (record p. 124) by stipulation of parties only for purposes of any computation under Rule 50, and which said evidence was not introduced nor available as the basis of any findings of fact in reference to the issues between the parties herein.

2. Petitioners move to strike from said findings of fact, the sentence "the cose to the corporation of the properties acquired by it was between $407,000 and $507,000", because said evidence was irrelevant and incompetent, and was received over the objections of petitioners.

3. That the Board erred in its conclusion of law that the agreements herein between the corporate petitioner and operating companies should not be held to be sales of coal in place, being the legal construction admitted to attach to said agreements under the laws of West Virginia.

4. That the Board erred in setting forth evidence in its opinion, concerning the value of the property on March 1, 1913, which evidence is not set forth in its findings of fact.

5. That the Board erred in not including in its find-
(69) ings of fact, that amount of the depletion allowable to the corporate petitioner is res adjudicata herein under the decision of Bankers Pocahontas Coal Co. vs. Albert White, Collector, and, also, under its findings of fact that the subject matter of said decision and the parties therein are identical with those involved in the present proceedings.

6. That the Board erred in stating in its opinion additional evidence as to the cost of the properties was introduced and also regarding the estimated tonnages in each of the leases; it appearing said evidnce was taken over the objections of petitioners upon cross examination by respondent, and otherwise was introduced subject to stipulation only for purposes of a Rule 50 computation.

7. That the Board erred in holding the damages recovered from the Flanagan Coal Company constitute a recovery of the value of coal mined, subject to allowance for depletion, as contradictory to its findings of fact thereon.

8. That the Board having erred as aforesaid, in its decision of the Bankers Pocahontas Coal Company appeal likewise erred in applying its principles to decision of the appeals of petitioner Strother.

And, it appearing this decision was reviewed by the Board, Petitioners request that this motion for rehearing and modification be reheard by the Board.

(s) CAMDEN R. McATEE,
Attorney for Petitioners.

(70) **ORDER**

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Co.,
Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 14516, 14517, 42664, 10472, 25275, 32170.

Counsel for petitioners in the above entitled proceedings having filed a motion with the Board on February 27, 1930, for a rehearing or for modified findings of fact and opinion as set forth in the report promulgated January 22, 1930, alleging that the Board erred in including in said findings of fact certain data contained in a stipulation which counsel now claims was introduced solely for purposes of any recomputation under Rule 50; that a certain findings of fact be stricken from the report on the ground that the evidence supporting said findings of fact was irrelevant, incompetent, and received over objection of counsel for petitioners; that the Board erred in several conclusions of law as set forth in its opinion and in not including in its findings of fact a certain other conclusion of law to the effect that the amount of allowable depletion is res adjudicata; that the Board erred in setting forth certain evidence in its opinion, and the premises considered and due consideration having been given thereto as well as to statements of counsel for the petitioners at the hearing in the above entitled proceedings and to his then position with respect to the matters presently complained of, and after reconsideration of the record herein, it is

ORDERED that the motion be and the same is hereby denied.

(Signed) CHARLES P. SMITH
Member,
United States Board of Tax Appeals.

Washington, D. C.

Entered: March 6, 1930.

CPS:aa.

NOTICE OF SETTLEMENT

(71) Filed Mar. 31, 1930.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner.

v.

Docket Nos.
14516-14517-42664

Commissioner of Internal Revenue,
Respondent.

The annexed proposed determination of deficiency under the opinion of the Board of Tax Appeals heretofore rendered herein will be presented to the Board for settlement on the .... day of ..... 1929, at 9.30 A. M.

This notice of proposed determination is submitted in accordance with the decision of the Board without prejudice to the Commissioner's right to contest the correctness of the decision pursuant to the statute in such cases made and provided.

(Signed) C. M. CHAREST
C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

OF COUNSEL:

MAXWELL E. McDOWELL,
FRANK B. SCHLOSSER,
Special Attorneys,
Bureau of Internal Revenue.

(72) STATEMENT
IT:AR:F-6
LGS

In re: Bankers Pocahontas Coal Company, Welch, West Virginia.

Docket Nos. 14516, 14517, 42664.

Years	Additional Tax
1920	$5,202.27
1921	7,849.75
1922	4,150.08
1923	4,102.78
1924	3,677.23
1925	6,855.09
1926	7,333.85
Total	$39,171.05

1920

Income 60-day letter		$44,907.86
Deduct:		
Depletion (Board's decision)	$16,423.02	
60-day letter	16,371.65	
Balance	$ 51.37	
Royalties	$5,434.66	
Taxes	180.00	
		5,666.03
Net income adjusted		$39,241.83

Invested Capital

60-day letter		$294,955.64
Add:		
Dividend adjustment,		
60-day letter	$20,130.33	
Board's decision	19,519.33	611.00
Invested capital adjusted		$295,566.64

Excess Profits Credit

8% of invested capital plus $3,000.00 equals	$26,645.33

(73) Computation of Tax

Income	Credit	Balance	Rate	Tax
$39,241.83	$26,645.33	$12,596.50	20%	$2,519.30

Net income adjusted		$39,241.83	
Less:			
Profits tax	$2,519.30		
Exemption	2,000.00	4,519.30	
Taxable at 10%		$34,722.53	3,472.25
Tax liability			$5,991.55
Previously assessed			789.28
Additional tax			$5,202.27

1921

Income 60-day letter			$47,022.84
Add:			
Depletion 60-day letter		$11,966.69	
Board's decision		11,921.87	44.82
Net income adjusted			$47,067.66

Invested Capital

60-day letter			$281,652.96
Add:			
1920 income tax prorated			
60-day letter		$3,206.20	
As corrected, $5,991.55 x .4226		2,532.03	
		$ 674.17	
Dividend adjustment			
60-day letter	$22,170.90		
Board's decision	20,452.62	1,718.28	2,392.45
Invested capital adjusted			$284,045.41

Excess Profits Credit

8% of invested capital plus $3,000.00 equals	$25,723.63

(74) Computation of Tax

Income	Credit	Balance	Rate	Tax
$47,067.66	$25,723.63	$21,344.03	20%	$4,268.81

Net income adjusted	$47,067.66	
Less:		
Profits tax	4,268.81	
Taxable at 10%	$42,798.85	4,279.89
Tax liability		$8,548.70
Previously assessed		698.95
Additional tax		$7,849.75

1922

Income 60-day letter		$61,947.12
Add:		
Depletion 60-day letter	$16,806.09	
Board's decision	16,799.36	6.73
Net income adjusted		$61,953.85
Tax at 12½%		$ 7,744.23
Tax liability		$ 7,744.23
Previously assessed		3,594.13
Additional tax		$ 4,150.08

1923

Income 60-day letter		$58,656.51
Deduct:		
Depletion Board's decision	$17,177.79	
60-day letter	17,090.60	87.19
Net income adjusted		$58,569.32

Tax at 12½%		$ 7,321.17
Tax liability		$ 7,321.17
Previously assessed		3,218.39
Additional tax		$ 4,102.78

(75) 1924

Income 60-day letter		$55,362.70
Add:		
Depletion 60-day letter	$23,073.93	
Board's decision	20,553.41	2,520.52
Net income adjusted		$57,883.22
Tax at 12½%		$ 7,235.40
Tax liability		$ 7,235.40
Previously assessed		3,558.17
Additional tax		$ 3,677.23

1925

Income 60-day letter		$49,377.26
Add:		
Depletion 60-day letter	$22,205.65	
Board's decision	18,851.47	3,354.18
Net income adjusted		$52,731.44
Tax at 13%		$ 6,855.09
Tax liability		$ 6,855.09
Previously assessed		None
Additional tax		$ 6,855.09

1926

Income 60-day letter		$52,879.06
Add:		
Depletion 60-day letter	$23,993.33	
Board's decision	22,547.56	1,445.77
Net income adjusted		$54,324.83
Tax at 13½%		$ 7,333.85
Previously assessed		None
Additional tax		$ 7,333.85

OBJECTIONS OF PETITIONER TO TAX DETERMINATION PROPOSED BY RESPONDENT, AND COUNTER DETERMINATION PROPOSED BY PETITIONER

(76) Filed May 21, 1930.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket Nos. 14516, 14517, 42664.

Commissioner of Internal Revenue,
Respondent.

The petitioner, Bankers Pocahontas Coal Company, without prejudice to its right to contest the correctness of the tax determination herein, pursuant to the statute in such cases made and provided, and with said right expressly reserved, objects and excepts to the deficiency computation of respondent proposed and filed herein on March 31, 1930 as being an erronous tax computation, for cause as follows:

1. For the years 1920 to 1926 inclusive, depletion has been computed at .036 per ton on the basis of tonnage mined each year.

In fact, petitioner received royalties in each of said years on tonnage in excess of the tonnage mined, said excess and the depletion thereon, being as follows:

	1920	1921	1922	1923	1924	1925	1926
Lease #1	62,811	65,340	64,136	68,578	62,072	51,196	29,971
Lease #3	300	1,712			12	75	1,647
Lease #4	13,082	84,703	9,821	3		8,830	554
Lease #4	168,269	281,226	324,950	266,630	339,780	207,208	181,398
Lease #5	1,913	1,511	162				
Lease #6		32,163	19,811	5,040			44,564
	242,549	399,307	359,616	330,171	401,864	267,164	254,840
@ .036	$8,731.76	$14,375.05	$12,946.18	$11,886,16	14,467.10	$9,617.90	$9,174.24

Petitioner states disallowance of depletion on tonnage paid for but not mined distorts the taxable income of petitioner by including therein royalty payments properly subject to a depletion allowance, and that the right of the operating companies thereafter to mine coal previously paid for was recognized and admitted by petitioner; that the findings of fact of the Board are erroneous in stating that a depletion unit of .036 per ton was allowed by respondent to petitioner in the several years only upon coal mined, and in fact a different rate was allowed in some of the years and applied to coal paid for, and not alone to coal mined, in the deficiency letters in evidence.

2. For said years 1920 and 1921, the computations of invested capital are dependent as to the item "Dividend Adjustment" upon the allowance of proper depletion deductions in the computation of taxable net income, (78) and the proper invested capital of petitioner for each of said years cannot be ascertained until the erroneous calculation of allowable depletion is corrected.

3. The tax liability for 1920 and for 1921 cannot be computed until the aforesaid items of correct taxable net income and invested capital are ascertained.

4. For the years 1922 to 1926 inclusive allowance of depletion as claimed in paragraph 1 hereof will compute the several deficiencies as follows:

	1922	1923	1924	1925	1926
Adjusted Net Income	$61,953.85	$58,569.32	$57,883.22	$52,731.44	$54,324.83
Additional Depletion	12,946.18	11,886.16	14,467.10	9,617.90	9,174.24
Revised Net Income	$49,007.67	$46,683.16	$43,416.12	$43,113.54	$45,150.59
Tax	6,125.96	5,835.39	5,427.02	5,604.76	6,095.33
Previously Assessed	3,594.15	3,218.39	3,558.17	None	None
Deficiency	$2,531.81	$2,617.00	$1,868.85	$5,604.76	$6,095.33

6. Petitioner moves the Board for amended and (79) supplemental findings of fact, and renews its

motion heretofore filed for a rehearing and reconsideration of the findings of fact and opinion of the Board herein.

WHEREFORE, petitioner prays the determination of deductible depletion at .036 per ton upon the tonnage paid for in the several years, the recomputation of dividend adjustments as a factor of invested capital for the years 1920 and 1921, the determination of any deficiencies for years 1920 and 1921 as the result of said adjustments, and the determination of any deficiencies for the years 1922 to 1926 inclusive in the amounts shown in paragraph four hereof, and for all other proper relief.

(s) CAMDEN R. McATEE,
Attorney for Petitioner,
1021 Tower Building,
Washington, D. C.

(80) **ORDER**

UNITED STATES BOARD OF TAX APPEALS

Washington

Bankers Pocahontas Coal Co., Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 10472, 14516, 14517, 25275, 32170, 42664.

At an oral hearing of these proceedings under Rule 50 of the Board's Rules of Practice on June 18, 1930,

counsel for the petitioners made a motion for a rehearing or reargument of the cases for the purpose of filing additional evidence and for the purpose of raising the question as to whether depletion should be based upon the tons of coal mined each year or upon the tons of coal paid for by the lessees each year. In its opinion the Board held in accordance with Littie A. Knapp, 7 B. T. A. 790, and A. T. Cooper, 7 B. T. A. 798, that the depletion deduction should be based upon the tons of coal mined. It is, therefore,

ORDERED that the motion for rehearing or reargument of the cases be and the same is denied.

(Signed) CHARLES P. SMITH
Member,
United States Board of Tax Appeals.

Entered: July 15, 1930.

CPS:aa.

(81) **DECISION**

UNITED STATES BOARD OF TAX APPEALS

Washington

Bankers Pocahontas Coal Co., Petitioner,

v.

Commissioner of Internal Revenue, Respondent.

Docket Nos. 14516, 14517, 42664.

Pursuant to the findings of fact and opinion promulgated by the Board in the above entitled proceedings January 22, 1930, counsel for the respondent, on March 31, 1930, filed a notice of settlement under Rule 50 of the

Board's Rules of Practice and, on May 21, 1930, counsel for the petitioner filed objections to "Tax Determination Proposed by Respondent and Counter Determination Proposed by Petitioner." The principal point of difference between the alternative notices of settlement is whether the depletion allowance should be computed upon the basis of coal mined each year or upon the basis of tons of coal paid for by the lessees each year. The Board held that the allowance for depletion should be based upon the tons of coal mined and the respondent's notice of settlement is computed in accordance with the opinion of the Board. A hearing on the redetermination under Rule 50 was had on June 18, 1930, at which counsel for the respondent and counsel for the petitioner admitted that the notice of settlement filed by the respondent was in accordance with the opinion promulgated. Wherefore, it is

ORDERED and DECIDED that there are deficiencies in income and profits tax for the years 1920 to 1926 as follows:

1920	$5,202.27
1921	7,849.75
1922	4,150.08
1923	4,102.78
1924	3,677.23
1925	6,855.09
1926	7,333.85

(Signed) CHARLES P. SMITH
Member,
United States Board of Tax Appeals.

Entered Jul 16 1930

CPS:aa

(82) **ORDER**

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Co., Petitioner,

v.

Commissioner of Internal Revenue, Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue, Respondent.

Docket Nos. 10472, 14516, 14517, 25275, 32170, 42664.

It appearing as a result of a hearing on the notice of settlement of the deficiencies of D. J. F. Strother, Docket Nos. 10472, 25275, and 32170, that there is an error in the last paragraph of the findings of fact of the Board, promulgated January 22, 1930, 18 B. T. A. 901, it is

ORDERED that the last paragraph of said findings of fact be deleted and that there be substituted therefor the following paragraph:

In the several years involved herein the petitioner, Strother, as one of the corporation's stockholders, received payments from the Bankers Pocahontas Coal Co. and reported same in his returns but did not return them as taxable income. The corporation received the royalties of the contracts, used such portion as was necessary for payment of the ordinary and necessary expenses of administering business, set aside a certain reserve to meet pending Federal taxes and distributed the rest to the stockholders. No allowance was made by the Commissioner to the petitioner, Strother, for any depletion

reserve received by him and the Commissioner added the entire receipts to his net income and has determined deficiencies accordingly.

(Signed) CHARLES P. SMITH
Member,
United States Board of Tax Appeals.

Washington, D. C.,

Entered September 26, 1930.

PETITION FOR REVIEW

(83) Filed Jan. 6, 1931.

CIRCUIT COURT OF APPEALS OF THE UNITED STATES
FOURTH CIRCUIT

Bankers Pocahontas Coal Company,
Appellant,

v. Docket No. .....

Commissioner of Internal Revenue,
Appellee.

Petitioner appellant, Bankers Pocahontas Coal Company, being aggrieved by a decision of the United States Board of Tax Appeals (hereinafter called the "Board") determining additional income and profits taxes of $39,171.05 and legal interest for the calendar years 1920 to 1926, inclusive, as entered on July 16, 1930, in the appeal of Bankers Pocahontas Coal Company v. Commissioner of Internal Revenue, No. 14516, 14517 and 42664 (consolidated) on the docket of said Board, hereby respectfully submits its petition for review thereof by this Court, and for cause in support thereof states as follows:

1. Now and at the times hereinafter mentioned peti-
(84) tioner appellant was and is a corporation organized under the laws of the State of West Virginia with its principal office in said state and within the jurisdic-

tion of this Court, and prosecutes this proceeding in its own right. Appellant is engaged in no business, and its only activity is the collection for and distribution to its stockholders of moneys payable by operating companies for coal taken by them from its properties. Appellee is the duly appointed and qualified Commissioner of Internal Revenue, and is joined herein as a party in his official capacity. For the several years 1920 to 1926, inclusive, petitioner appellant filed its returns for income and profits tax determination and assessment with the Collector of Internal Revenue at Parkersburg, West Virginia, which office is within the Circuit of this Court, and whereby jurisdiction of this petition for review is claimed pursuant to Section 1001-2 of the Revenue Act of 1926.

2. For the calendar years 1920 to 1926, inclusive, appellant made and filed its income and profits tax returns to disclose its gross income and the deductions (85) and credits against same allowed by the several Revenue Acts, as computed upon a cash receipts and disbursement basis, and to permit assessment of tax upon the resulting income, if any, and paid any tax shown thereby for each of said taxable years.

3. (a) In each of said taxable years the major portion of the gross income of appellant, and which is here in controversy, consisted of money payments received from certain original operating companies, or their successors in interest, under contracts, for the mining and taking of coal by them from the lands owned in the several years by appellant before March 1, 1913, and which contracts were made and existing with the predecessors of appellant, and were acquired by appellant before March 1, 1913, and have since been owned by appellant. Exclusive of the coal content thereof so contracted to be taken and paid for by said operating companies, said lands owned by appellant were and are without value. Appellant reported said money payments in its several returns as gross income received each year, but did not include same in its several returns as any part of taxable net income for cause that appellant claimed and alleged said money payments were the (86) proceeds of sales of coal in place effected and de-

termined by said contracts before March 1, 1913, and thereafter continuing, and that consequently no part of said payments was subject to any income and profits tax under the Sixteenth Amendment to the Constitution of the United States.

(b) In the taxable year 1924 appellant received $3,770.40 in settlement of its action for damages as the result of a trespass in 1920 upon its property by a certain operating company and a taking of its coal to an unascertained extent, said operating company having no contractual relation with appellant, and having destroyed its entries so the extent of its trespass and taking of coal could not be ascertained. Appellant reported said payment as gross income, but did not include same in its return for 1924 as any part of taxable net income on the ground and for cause that same constituted a replacement of capital to the extent of the amount received.

4. Upon review and examination of said returns of appellant, the appellee, Commissioner of Internal Revenue, ruled that the money payments to appellant in the several years from the operating companies constituted payments of royalties by lessees to a lessor and were (87) not proceeds of a sale of coal in place, and that said receipts were taxable to appellant in the years received to the extent same exceeded any return of capital therein received, and that said return of capital or depletion amounted to an average amount of 3.6¢ per ton of coal for the years 1920-1923 and for the years 1924-1926 amounted to varying individual amounts for each operation, averaging 2.6¢ per ton of coal paid for. Appellee further ruled the 1924 damages of $3,770.40 constituting income after deduction therefrom of capital or depletion at the rate of 3.6¢ upon 15,000 tons of coal. The taxable net income reported by appellant in its several returns was accordingly adjusted and increased, and the resulting deficiencies in tax were proposed against appellant by official letters from the appellee Commissioner.

5. Whereupon, within the time and as allowed by law, appellant, alleging error of law and fact therein on the part of appellee Commissioner, appealed to said Board

from said official findings as to each of said adjustments and the resulting tax proposals, praying a redetermination thereof, and issue was joined on said appeals by answers filed by appellee Commissioner.

6. At the consolidated hearing of said appeals by (88) the Board on May 3, 1929, appellant presented evidence to show said proposed deficiencies were erroneous and contrary to law.

Appellant alleged said money payments were proceeds of sales of coal in place contracted for before passage of the Sixteenth Amendment, and by agreement of the parties a typical contract was stipulated in evidence on said issue; appellant further alleged in the alternative that if appellant and said operating companies were lessor and lessees under said contracts, in such event the depletion rates proposed by appellee Commissioner were erroneous because previously established to be 5¢ per ton. Upon this issue appellant offered in evidence the proceedings in an action at law by appellant in the United States District Court for the Southern District of West Virginia against the Collector of Internal Revenue for recovery of income and profits taxes for the years 1914 to 1919, inclusive, alleged to have been erroneously and illegally determined and collected through use of 3.6¢ per ton as the depletion rate, wherein the opinion and judgment of the court was that appellant in the computation of said taxes was entitled to a deple- (89) tion rate of 5¢ per ton, and a recovery of said taxes was thereby adjudged and paid, and which judgment has always been in full force and effect, and finally established said depletion rate between the parties. Appellant further offered testimony that the damages of $3,770.40 received in 1924 had no relation to mining of any determinable quantity of coal.

At the end of the hearing, by agreement the parties stipulated of record for use in the computation of deficiencies, if any, after decision of the appeals by the Board, schedules showing the contracts upon the several coal properties of appellant, the estimated recoverable tonnage therein on March 1, 1913, and the tonnage mined and money payment received as to each property for the calendar years 1913 to 1926, inclusive.

7. Thereafter, the findings of fact and decision of the Board, promulgated on January 22, 1930, approved the determination of the appellee Commissioner that the money payments to appellant from said contracts were royalties of a lessor subject to allowance for depletion of the property from which derived; that the rate of 3.6¢ per ton of coal mined, found to have been deter-
(90) mined by appellee Commissioner, was a reasonable depletion deduction in the several years, and that the damages received in 1924, less depletion, were taxable income in the absence of evidence that the tortuous taking of coal in 1920 established an ascertained loss, or that the value of the coal taken exceeded the depletion allowance.

8. Appellant filed its motion to set aside and modify said findings of fact and decision and for a rehearing, and same was overruled without hearing.

9. A proposed determination of tax pursuant to said findings and opinion being offered by appellee Commissioner, appellant filed its objections and counter proposal and the parties were heard. It appeared therein from both parties as revealed by the deficiency letters the Board finding that depletion was computed by appellee Commissioner upon coal mined was in error, and that depletion had been computed on coal paid for, and appellant tendered and offered in evidence contracts or leases to show the payments per ton by operating com-
(91) panies permitted the mining of the coal at any time thereafter. Said contracts we excluded upon objection of appellee, and the Board took the matter of reopening and rehearing the appeals under advisement. Thereafter on July 16, 1930, the Board approved and ordered the determination of deficiencies proposed by the appellee Commissioner to be entered in the following amounts:

1920	$5,202.27
1921	7,849.75
1922	4,150.08
1923	4,102.78
1924	3,677.23
1925	6,855.09
1926	7,333.85

10. Appellant states the true determination of its gross income from said contract money payments as taxable or non-taxable, and of the amount of depletion, if any, to which appellant may be entitled, is necessary properly to ascertain its liability for taxes in the several years, and also to ascertain the liability for taxes therein of its several stockholders to whom said gross income is distributed by appellant.

11. Appellant states the Board in its findings of fact found as follows upon the issues herein presented, to (92) which findings appellant offers no objection.

"In July, 1912, the Bankers Pocahontas Coal Co., a West Virginia corporation (hereinafter sometimes called the corporation), acquired the fee simple title to approximately 6,200 acres of coal lands, including both the surface and the mineral rights in the State of West Virginia. The land had no appreciable value except for the coal content.

"Upon incorporation in 1912, the corporation acquired by formal assignment and has continued to retain the beneficial interest of the original owners in certain contracts affecting the coal content which were executed in 1901 and 1902 with various operating companies and to which contracts the 6,200 acres and coal content were subject.

"These contracts were originally prepared by D. J. F. Strother, who at that time was attorney, director, and stockholder in the predecessor corporations. The form of the contracts is that prevailing in the West Virginia coal fields, which followed the Pennsylvania form of contracts as introduced by Pennsylvanians who were largely instrumental in the early coal development in the West Virginia field.

"By agreement of parties a copy of such contracts was offered and received in evidence as typical of the several contracts existing on the acreage acquired by the corporation in 1912. The specimen contract provides in part as follows: (Contract inserted.)

* * * * *

"All of these agreements were in the main, with the (93) exception as to minor and non-essential provisions, the same as the sample agreement set forth above as the Cletus lease.

"From time to time these agreements were reassigned by the lessees to new and different operating leases, largely with the permission of the lessor corporation."

* * * * *

"In the several taxable years in controversy the corporation was upon a cash receipts and disbursements basis of accounting and its income, except minor items not in controversy, consisted of payments received under the several contracts from the various operating companies, and income and profits-tax returns were filed for each of the taxable years and thereafter audited by the Commissioner resulting in the deficiency notice forming the basis of the present proceedings."

* * * * *

"For prior years 1914 to 1919, inclusive, the Commissioner proposed additional taxes in the amount of $6,267.08 and required the corporation to pay same, which thereafter brought an action on February 17, 1923, in the United States Court for the Southern District of West Virginia against the collector to recover same on the grounds that payments under said contracts received by the corporation were the proceeds of a sale of coal in place consummated before March 1, 1913, or of choses in action existing on said date, or that petitioner plaintiff, as a lessor, was entitled to a unit depletion rate of not less than $0.05 per ton mined in the computation of net taxable income, and consequently said taxes were erroneously and illegally assessed and collected. The (94) issues were made in said action, and same were submitted for judgment upon the evidence adduced by the parties, and were decided by opinion of the court and judgment entered thereon that petitioner plaintiff in the computation of said taxes was entitled to a depletion unit of $0.05 per ton instead of $0.036 computed

by the Commissioner. A recovery of $5,373.01 from said collector by petitioner plaintiff was adjudged and said judgment was duly paid by the United States. In said action the Bankers Pocahontas Coal Co., one of the petitioners herein, was plaintiff; plaintiff petitioner appearing in its own right and the collector as defendant, who was defended in said action by the United States District Attorney and the Solicitor of Internal Revenue (now General Counsel). In this proceeding and in said court action the subject matter of the action and of these proceedings is the same, namely, the depletion unit allowable in computing the amount of such depletion deduction as will return to the taxpayer the capital value existing in the coal content of the corporation's property as of March 1, 1913."

* * * * *

"In 1920, the Flanagan Coal Co., which owned land adjacent to the petitioner corporation, trespassed on the land of the petitioner corporation and removed coal to which it had no right. It then destroyed the entries so that the damage or extent of the operation could not be determined. The corporation discovered the situation in 1923 and brought suit for damages and, as a result of a compromise of the suit, received in 1924, $3,770.40 in settlement and adjustment of the controversy. The petitioner corporation had no contractual relation with the trespasser and the settlement had no relation to the coal (95) extracted, as the amount of same could not be determined. The Commissioner held the damages received were equivalent to a royalty and adjusted same by the allowance of $0.036 per ton as depletion on 15,000 tons estimated to have been damaged or removed by the trespasser."

12. Appellant further states the Board in its findings of fact found as follows upon the issues herein presented, to which findings appellant offers objection:

"The cost to the corporation of the properties acquired by it was between $407,000 and $507,000.

"The contracts of the property on March 1, 1913 are

shown by the following: Schedule 1 (Details here omitted).

"The estimated recoverable tonnage on March 1, 1913, is shown by the following: Schedule 2 (Details here omitted).

"The tonnage mined and royalty receipts of the corporation for the years 1913 to 1919, inclusive, is shown by leases as follows: Schedule (Details here omitted).

"The tonnage mined, the tonnage paid for, and the royalty receipts for the taxable years involved in these proceedings are shown by the following: Schedule (Details here omitted).

* * * * *

"In computing the deficiencies the Commissioner con-
(96) sidered the relation of the corporation and the operating companies to be that of lessor and lessee and allowed the corporation a depletion deduction of $0.036 per ton mined for the years 1920 to 1926, inclusive, the same depletion rate as was allowed by the Commissioner for 1919 and prior years."

13. Appellant believes and avers that errors of law and fact were committed by the Board in its aforesaid findings of fact, decision and determinations to the damage and prejudice of appellant, as shown by the following

ASSIGNMENT OF ERRORS

1. In its ruling that the payments to appellant by the operating companies under the typical contracts are part of the gross income of appellant subject to tax, and are not income exempt from tax because realized from a sale of coal in place completed before March 1, 1913.

2. In its ruling that the judgment of the United States Court of West Virginia was not conclusive that a depletion rate of 5c per ton was available to the appellant in the subsequent taxable years here involved.

3. In its admission and use of alleged additional evidence of the cost of the properties, to which objections (97) and exceptions were made at the time of offer of same, and of tonnages in each of the several properties, which schedules were offered solely for possible computations of the taxes, if any, determinable under the decision of fact and law otherwise to be made by the Board, and in its failure to exclude and disregard said alleged additional evidence.

4. In its ruling that the damages received in 1924 constituted income subject to depletion and not a replacement of capital.

5. In its ruling, refusing to reopen or modify its findings of facts and its opinion or grant appellant any rehearing, made in overruling the motion of appellant therefor.

6. In its ruling and refusal to reconsider and correct its finding that 3.6c per ton mined was applied by appellee Commissioner in the several taxable years.

7. In its ruling and refusal to receive evidence to establish that coal paid for should be established as the (98) basis of depletion instead of coal mined.

8. In other respects apparent of record.

WHEREFORE, your petitioner appellant prays that the aforesaid decision and determination of said Board entered as aforesaid be reviewed and reversed by this Honorable Court, and for all other and further relief as the Court shall deem meet and proper in the premises.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Appellant.

District of Columbia:

CAMDEN R. McATEE, being duly sworn, deposes (99) and says that he is one of the attorneys for the

petitioner appellant; that he knows the contents of the foregoing petition; that to the best of his knowledge and belief the statements therein are true, and that the assignments of error are well taken, and intended to be argued.

CAMDEN R. McATEE,

Subscribed and sworn to before me this 6th day of January, 1931.

ETHEL R. GUISE,
Notary Public.

(SEAL)

NOTICE AND SERVICE OF PETITION FOR REVIEW

The General Counsel (Hon. C. M. Charest), Bureau of Internal Revenue, Washington, D. C., will please hereby take notice—

That on January 6th, 1931, a petition for review by the Circuit Court of Appeals of the United States for the Fourth Circuit of the Board decision and determination in the above entitled appeals was filed with the Clerk of said United States Board of Tax Appeals, and a true copy of said petition is herewith served upon you.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioner.

Service of above notice and receipt of copy of petition for review is hereby acknowledged this 6th day of January, 1931.

C. M. CHAREST,
Attorney for Appellee.

STATEMENT OF EVIDENCE

(100) Filed July 14, 1931.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket Nos. 42664, 14516-7.

Commissioner of Internal Revenue,
Respondent.

At hearings of the above entitled appeals, (consolidated for hearing) on May 3, 1929, and at subsequent adjournments thereof, before Hon. C. P. Smith, Board Member, the following proceedings were had and evidence offered material to the issues presented by petitioner as appellant in its petition for review of said appeals by the United States Circuit Court of Appeals for the Fourth Circuit.

To maintain the issues on its part joined, petitioner offered oral testimony of its witness D. J. F. Strother, President of petitioner, and various written records as exhibits, and respondent to maintain the issues on its part joined, offered oral testimony of said Strother.

The substance of the testimony given by said witness, (101) of the exhibits introduced, and of the proceedings herein, was and is as follows:

D. J. F. Strother: I am a lawyer and banker, and am President of the Bankers Pocahontas Coal Company since its organization, and am practically the whole thing. This company was organized in 1911-1912 under the laws of West Virginia, and the property was previously held for a year in the name of trustees. Its gross acreage is approximately 6,000 acres, valuable for the coal that is apparently in the property, and exclusive of the coal content it has no value. When the property was acquired in 1912 it was subject to certain contracts which

were acquired by the company, together with the beneficial interest in same, and the fee simple title to the land. The interest so acquired in the contracts was that of an owner, allowing another person to operate the coal property, and that right or beneficial interest as an owner has since been held by the company. I am familiar with the lease known as the Cletus lease, and attached as an exhibit copy to the petitioner's appeal No. 14517, having prepared that lease; and with the consent of the respondent I identify and offer said lease in evidence as "Strother (102) Exhibit No. 1." Said lease is set forth in full in the Board's findings of fact (18 B. T. A. 901,903), and reference is made to same for all purposes. The Cletus lease was drawn by me on or about June 17, 1901 while I was practicing law in the neighborhood of these properties; while I was personal counsel for the owners of the company, and also a stockholder and director. This was the first work I did in West Virginia. The form of the Cletus lease is the same as prevailed at that time in the West Virginia coal fields, and I was familiar with the leases in use there at that time. Such leases follow the Pennsylvania form, because whole sections of the country were largely developed by Pennsylvanians who brought their traditions with them. The other contracts upon tracts of land included in this 6,000 acres owned by the company, are substantially the same in form as this Cletus lease; the only substantial difference would be the royalty rates; although there may be a good deal of difference in the wording, but they all go through in the same way and I would say the Cletus lease is a typical form. I am not quite sure whether the Cletus lease provides for mining of seams of coal subsequently discovered and not known at the time the contract was made, but later contracts so provided, and some of them pro- (103) vided that if additional seams of coal other than that being mined or developed at the time, were discovered, the operator would have the right to operate those additional seams, provided he did so within a certain specified time. The lease fixed a minimum rate per ton in the contract to be paid by the operator, and specific rates for the mining of coal in additional seams were to be determined at a later time.

The parties stipulate said Cletus lease shall be con-

sidered as the typical instrument or contract upon the legal issue of whether or not a sale of coal in place was accomplished under the several instruments or leases acquired by the Bankers Pocahontas Coal Company.

The parties further stipulate the several deficiency letters of which copies are attached to the petitions of the Bankers Pocahontas Coal Company were duly received by said company, and showed the deficiencies therein (104) stated.

The parties further stipulate the gross income of the Bankers Pocahontas Coal Company for each of the several years in controversy was derived from payments made under the several contracts upon its land in reference to the coal content of same, excepting any items otherwise appearing in the original returns filed herein, and that in any computation under Rule 50, said returns may be used as though offered in evidence in this proceeding.

The returns of the company were made on the basis of money actually received; that is, a cash receipts and disbursement basis.

CROSS EXAMINATION

State and county taxes against the property are assessed against the Bankers Company, and the operating companies are billed for the taxes based upon the acreage controlled by them. I do not believe we have failed to get any taxes at all, except from one company last year, 1928. The Bankers Company at all times followed (105) the general custom of protecting its interest by seeing that taxes were paid on the property, as they owned the land and had to pay the taxes.

RE-DIRECT EXAMINATION

The 1928 item of taxes not repaid to the Bankers Company still remains unpaid.

Re-Cross Examination

The Bankers Company acquired this contract of about 6,200 acres in 1911, and the deed to the company was made in July, 1912. When the deed passed the title of properties to the company, these operating contracts were already in existence, and riding the property so to speak, and had been in existence since 1901, 1902 and 1903. The Bankers took the property, plus the contracts, and there was a subsequent formal re-assignment of the contracts and acquisition of them by the Bankers Company in its own name.

Witness being asked by respondent's attorney for the consideration paid for its land by the Bankers Company, and having answered he could give a pretty good esti-
(106) mate, attorney for the petitioner objected that only the legal nature of the contract is involved, and cost is not material, and that no issue in the case goes beyond the basic date of March 1, 1913. The Board member overruled the objection and granted an exception to the petitioner from said ruling.

My recollection is a bond issue was outstanding on the property at that time of either $240,000 or $260,000. We paid out $60,000 in cash. There were some title troubles and we paid on that, considering that the stock at par, $35,000, and we lost, to straighten these titles out to the Standard Pocahontas Coal Company, 600 acres of coal, which we valued anywhere from $50,000 to $150,000. We settled two or three other claims of about $2,000 or more. I consider all these items to be consideration approximately given by the Bankers Company for the acquisition of this plot of 6,200 acres.

Thereupon, petitioner's attorney moved to exclude and strike out the answer of witness on the same grounds
(107) offered as objections to same, and the Board member denied said motion to strike.

Re-Direct Examination

In 1923 the Bankers Coal Company sued A. B. White,

Collector, in a District Court of the United States for West Virginia, for the recovery of income and profits taxes for the years 1914 to 1919 inclusive. In that action a contention was made concerning the amount allowable as a depletion unit. The action was tried upon a stipulation of facts and evidence of each party as to the valuation of the property and the determination of the depletion Unit. In deciding the case, the Court made a decision upon the question of the value of the property and the depletion unit, and a judgment was entered pursuant to its opinion, which judgment was subsequently paid. In said action the Bankers Pocahontas Coal Company sued in its own right, and is the petitioner in these proceedings. The subject matter involved related to depletion value under the provisions of Revenue Acts concerning income and profits taxes for the several years involved. Said depletion unit had reference to the same 6,200 acres involved in this proceeding. The same parties and the same subject matter were before the United States Court as appear in this proceeding, excepting (108) the Collector was the party defendant there, and in this proceeding the Commissioner is the respondent.

I have here a copy of the record in the West Virginia proceeding, attested as required by the Acts of Congress, and I identify and offer same in evidence, the record being marked "Petitioner's Exhibit 1," and the judgment in said proceeding being marked "Petitioner's Exhibit No. 2" for identification.

Thereupon, respondent's attorney stated any objection to the acceptance of said exhibits in evidence on the issue of res adjudicata is withdrawn, but objection is made to the utilization of the material, affidavits, Revenue Agents' reports, etc., appearing in the record as proof of specific facts in the case.

Thereupon, the presiding member received said exhibits as being certified copies of Court records that do not bind the Board to any doctrine of res adjudicata.

A summary of Petitioner's Exhibit No. 1, being the (109) record in the action styled No. 868, Bankers Pocahontas Coal Company, vs. Albert B. White, Collector of Internal Revenue in the District Court of the United

States for the Southern District of West Virginia, omitting praecipe, summons, and similar incidental matters, is as follows:

"1. Declaration filed February 21, 1923, in the Northern District at Parkersburg, West Virginia, claims the recovery from defendant of $6,267.08, being additional income and profits taxes for the years 1914 to 1919, inclusive, alleged to have been erroneously and illegally assessed against and collected from the plaintiff corporation, and which were paid under protest by said plaintiff on August 17, 1921, and for which a claim for refund was filed and rejected by the Bureau of Internal Revenue on or about April 5, 1922. To said declaration was attached a statement of account including, as part of same, Departmental letter of March 8, 1921 from the Commissioner of Internal Revenue, in which the adjustments relating to the tax determination for each year were specifically stated, including a determination that the depletion allowed is based upon a rate of 3.6c a ton mined as computed upon data submitted by plaintiff to said Bu-
(110) reau.

2. Consent order of September 3, 1923, transferring said case to the Southern District of West Virginia for trial, with transmittal of all original papers and a copy of said order to the Clerk of the District Court of the Southern District of West Virginia for further proceedings.

3. Consent order by attorneys for plaintiff and the District Attorney of the United States for said Southern District of West Virginia and by the special attorney for the Bureau of Internal Revenue, representing the defendant, agreeing to the jurisdiction of the United States District Court for the Southern District of West Virginia, and entering the appearances of their respective clients; said order further grants leave to the defendant to file its plea in writing, and same being filed, the plaintiff replied generally thereto; defendant having further pleaded the obligations set out in the plaintiff's declaration were not assumed or undertaken by defendant, and the parties having put themselves upon the country, and issues being thereupon joined, the parties tendered an

agreed statement of fact and other evidence, including deeds, coal contracts, engineering reports, deficiency letters, tax returns, protests and other writings, and all of (111) same were ordered filed and made part of the record herein, as the evidence in the case, and the parties being heard, time was taken by the Court for consideration of its judgment.

4. Agreed statement of fact that plaintiff corporation was organized in 1912 in West Virginia and by deed of July 19, 1912 acquired approximately 6,000 acres of West Virginia coal land for good and valuable considerations not specifically described in the deed of conveyance, and which lands were and are of practically no value excepting as to the coal content; said lands before March 1, 1913, were disposed of by several written instruments providing for payments of annual minimum amounts and a fixed payment per ton as to the respective acreage parcels, which writings were made by predecessors in title of the plaintiff, and all interest and benefits of which were paid to plaintiff by its deed of conveyance and otherwise; that when said written instruments were made the party known as lessees therein, took actual possession of the respective properties and continued to mine coal therefrom, and said parties, their successors and assigns have been continuously in said possession and mining, removal, and sale of the coal in said properties, (112) and are now so doing and paying to plaintiff the sums provided for in said writings; that since its organization the plaintiff has had no business, excepting the receipt of payments under said writings and distribution thereof to its stockholders, and all sums of money coming to plaintiff from any source, are those called for in said writings; that as of December 31, 1917, representatives of the Bureau of Internal Revenue examined plaintiff's property, books and records, and gave to plaintiff a report based thereon, as a basis for computing income and profits taxes, and thereafter, on June 18, 1918 said representative submitted a detailed report in pursuance of said examination; said 1917 report determined the 6,000 acres of plaintiff on March 1, 1913, had an estimated value, computed as 20,000,000 tons of coal at 5c per ton, or $1,000,000, and that the depletion reserve upon 1,517,435 tons removed in 1913 to 1917, inclusive,

at 5c per ton amounted to $75,871.75, and using said determination computed additional taxes to be due from plaintiff for the years 1914 to 1917 inclusive, of $379.17; said report of June, 1918, included detailed explanation of said preliminary findings, and that the estimated coal content of March 1, 1913 was conservatively determined in June, 1915 by a mining engineer representing third (113) parties; that if transmittal of said Departmental report of 1918 to the Commissioner of Internal Revenue, and review thereof, plaintiff was advised additional taxes were proposed for the years 1914 to 1918 inclusive of $2,-728.45, therein, depletion was allowed upon a rate of 3.6c per ton mined, as computed upon data submitted by plaintiff and said additional taxes so ascertained, were assessed against plaintiff for the several years; that plaintiff, as the result of conference with the Department in May, 1920, was requested to and did file with the Department its protest; that the valuation of said property by the Department to be $1,000,000 as of March 1, 1913 was reasonably correct, and that the payments under the written contracts of plaintiff were the proceeds of sales of coal in place consummated before March 1, 1913; the Departmental estimate of recoverable tonnage was insufficient, and the Departmental value of $510,000 at 3.6c per ton mined was not commensurate with the value of the properties or of similar property as known on March 1, 1913; that as the result of said protest, another Departmental investigation and report was made in verification in October, 1920, and which report referred to Departmental failure to value coal seams below water level, and that such seams required valuation, because (114) same were being mined; that thereupon, in March, 1921, the Department recomputed the taxes of plaintiff for the years 1914 to 1919, to be $6,267.08, instead of amounts previously proposed, and plaintiff protested said additional taxes and the valuation findings, used as the basis of the Departmental rate of 3.6c-per ton mined; that the several original tax returns of plaintiff for the years 1914 to 1919 inclusive, were exhibited as part of said agreed statement; that the Departmental determination of the March 1, 1913 value of plaintiff's coal property included consideration of data and reports as follows: Form B-MMS in reference to adjustment of invested capital by establishment of a paid-in surplus as

existing; Form A-MMS, being depletion schedule for 1909-1917; Strother and Hughes statement of March, 1919, giving history of plaintiff and summarizing valuation reports of various engineers made in the years 1907 to 1917, inclusive; engineer Doe's report of 1907, describing property, coal seams and conditions, operations, costs, sales and facilities; engineer Merrill's report of August 22, 1919, upon the same subjects, and ascertaining estimated content of 66,838,000 gross tons, of which 90% would be recovered through good mining practice; en-
(115) gineer Buck's report of June 23, 1915, covering said subjects and indicating royalty receipts for 25 years of $1,400,000 upon a 90% recovery basis; Engineer Hanlon's report of September 22, 1908 covering the same matters; that in reply to plaintiff's protest of March, 1921, against additional assessment of $6,267.08, on June 3, 1921, the Department affirmed its previous position that the evidence submitted was practically the same as previously considered, and justified no change in valuation, and further stated the sale of coal in place ruling was inapplicable for purposes of the Federal income tax; that said additional taxes were paid under protest of September, 1921, and a claim for refund thereof was filed; that the Departmental determination of depletion to be 3.6c per ton, consisted of conclusions as follows:

"1. It is desired to determine the value of the recoverable coal as of March 1, 1913.

2. This company sets up that on July 16, 1912, it acquired 6,138 acres of coal land, assuming a mortgage of $300,000.00 and litigation costs of approximately $150,000.00, or at a total cost of approximately $450,000.00; (116) which land was assessed at $156,392.00. The company is a coal land lessor having 5 operating coal lessees, with an average royalty of 8½ cents per ton, and a minimum of $33,000.00 per year. As of March 1, 1913, they claim 20,000,000 tons of recoverable coal valued at $1,000,000.00 with a 5 cent rate of depletion, endeavoring to substantiate their claim by 3 appraisals widely differing both in values and tonnage.

3. The lessees were operating when the purchase was made, that from 1909 to 1916, inclusive, the average an-

nual tonnage was 290,000 tons; yielding an income of $32,000.00, and even in 1917 the annual tonnage was but 360,000 tons, income $32,000.00, in no cases equal to the minimum royalty; that adjoining land (including the (117) coal) sold for $100.00 per acre, and that the showings both prior to and after March 1, 1913 do not tend to enhance the value of the coal.

The property carried 4 seams of coal; 2—Pocahontas No. 3 and No. 4 which are 300′ below water level, not worked on the property here, only a prospective value and both of these seams are diminished in thickness from 11 to 4½′ (with a band of 6′ slate) as they approach this property. No valuation of them is here made.

The No. 6 and No. 7 seams spoken of as the "Pocahontas thin vein" are both worked on the property. They vary from 30″ to 4½′, including the parting from 2″ to 6″, are about 200′ above the railroad, and underlay some 4,000 acres, but are so irregular and distributed that both are not uniformly worked, and a total of 14,000,000 tons (118) of recoverable coal is believed fair.

Therefore, taking the 14,000,000 tons recoverable coal; average annual tonnage of 350,000; an average annual income therefrom of $34,000.; a life of 40 years, we have a value of the recoverable coal of $510,000., or $.036 per ton.

4. It is therefore recommended that the rate of deple- (119) tion be fixed at $.036 per ton."

that the refund claim of plaintiff was rejected by the Commissioner; that Treasury decisions 2746 and 3107, and Article No. 244(d) and (e) of Regulations 62 be read in evidence; that the defendant Collector resides in, and has his office in the Northern judicial district of West Virginia, and the money sued for be paid for him as such Collector; that all profits and gains of plaintiff, and increases in the value of its property, arise by and through said instruments of writing; that objection by plaintiff to Treasury Decisions 2746 and 3107 are reserved as being of no probative force as evidence; that all exhibits filed with said statement may be considered as evidence

to determine any and all questions, the Court giving to any such paper such probative weight as if the writer thereof were under oath and testifying to same, and give to such evidence the weight he may think it entitled to.

5. Opinion by the Court:

This is an action at law to recover $6267.08 from the Collector claimed as a payment erroneously and illegally assessed and collected from the plaintiff.

It covers a period of six years, from 1914 to 1919 in-
(120) clusive.

All the necessary preliminary actions were taken by the plaintiff, and the action was properly brought.

The plaintiff is the owner of about six thousand acres of land, claimed to be underlaid with seams of coal, situate in McDowell County, West Virginia. This land was purchased in July 1912. Sundry coal leases covered the entire acreage at the time of purchase. Therefore, all that the plaintiff purchased, was the reserved rentals and royalties, as set out in the various coal leases. These varied. Some were for ten cents per ton, some for eight cents, some for seven cents, and one was for five cents. It is agreed that the land has no value, other than its coal.

This brings on the first contention of the plaintiff, that is, that the plaintiff, by the reserved rentals and royalties, is being paid for the land and the coal there-
(121) under, and that such rentals and royalties are not "income" but "purchase money".

Personally, I believe this statement to be true, but I cannot, in the face of all the decisions, sustain it here. I therefore hold, that the royalty payments are income, and should pay a tax as such.

Other items are in dispute in this case, and they will be taken up.

1st. The lessees of the plaintiff agreed, each for itself, to pay the state, county and district taxes assessed upon the land as described in each lease, and the plaintiff was thus wholly released from the payment of any such taxes. The payment thereof by the lessees, was a part of the purchase price of the coal, in addition to the

amount per ton, for all coal mined by each lessee. However, under the tax laws of West Virginia, the land was (122) charged to the plaintiff, and the collecting officer looked alone to the plaintiff for the payment of such taxes. In order to protect its property, and properly distribute the amount to be paid by each lessee, it was necessary that the plaintiff pay to the sheriff such taxes in bulk, and then collect from each lessee his distributive share thereof. These taxes have no place in the income tax accounts, unless lessee failed to reimburse the plaintiff, for the amount so advanced for it. In that event, such amount would be either a tax paid, for which the plaintiff would be entitled to a deduction as such, or it would be a lost debt, charged off, and in either event, the final result would be the same. The returns are somewhat confusing, because the taxes are credited as a deduction, and when repaid, are charged as income. From the proofs here, I cannot decide the exact state of the account thereof.

2nd. The value of the property as of March 1st, (123) 1913.

The valuation department of the office of the Commissioner values it as of the value of $510,000.00, and fixed the value of the depletion at $.036 per ton. After considering the proofs herein on that subject, and drawing the conclusions therefrom, in the light of forty years experience in observing such things in Southern West Virginia, I am of opinion, and hold, that the property has more tonnage of recoverable coal than has been allowed, although I do not believe that any lessee will ever recover ninety per cent of a coal seam.

I am of opinion that the depletion value should be at the lease five cents per ton, and that all the returns should be made on that basis.

3rd. I am unable to agree that attorneys fees paid by the plaintiff, are part of the capital account, and hold (124) that they are expenses, and should be allowed as such.

4th. Interest paid on debts, should be allowed as a deduction, and where plaintiff was primarily responsible,

and paid interest on a bonded indebtedness, it had the duty to pay it, and if any part thereof was not collected or collectible from the other party, then such interest, so paid, was a proper deduction.

5th. Under the head of expenses, I am at a loss what to take as correct.

Plaintiff by its president and secretary, make returns for these six years, and these officers, both well known to the court as men of probity and ability, swear to the correctness thereof. An agent or two comes along and says that certain amounts of expenses should be disallowed. In most instances here, there is no satisfactory explanation for such action, and no reason is given.

As the case stands here, I will accept the return of (125) expenses, and will allow the same, unless it affirmatively appears what such expense is, and it then shall appear improper.

From what has been said, I leave it to the counsel for the plaintiff and defendant, to draw a proper judgment in this action.

6. Tax recomputation pursuant to memorandum opinion, allowing depletion at the rate of 5¢ per ton, and including recapitulation of correct tax liability in comparison with taxes paid for the several years, and the resulting amounts of recoverable taxes and interest in said total recovery of $5,373.01.

7. Judgment, September 21, 1927.

This day came the parties hereto, by counsel, and the parties having agreed upon the facts, as set forth in (126) the order of this court, entered on October 10, 1923; and, trial by jury having been waived; and, the matters of law and fact having been submitted to the finding of the court, in lieu of a jury; and, the court having heard the argument of counsel—on briefs and orally—for the parties respectively; and, having maturely considered of his ruling and judgment herein; this day filed and made part of the record herein his opinion in writing. Whereupon in accordance with the terms and tenor of the written opinion of the court, the

court doth find that the defendant is indebted to the plaintiff, on account of excess taxes paid by the plaintiff to the defendant for the years 1914 to 1919; both inclusive, in the declaration mentioned, in the sum of $5,373.01, and doth assess the plaintiff's damages accordingly.

(127) WHEREUPON, IT IS ADJUDGED, ORDERED AND DIRECTED that the plaintiff do recover of and from the defendant, the sum of Fifty-three Hundred and Seventy-three and 1/100 (5,373.01) Dollars, with legal interest thereon from this date until paid, together with costs, to be taxed by the Clerk of this court, to the ruling of the Court in his findings herein and in entering judgment for the plaintiff the defendant at the time excepted.

The defendant announcing a desire to apply to the Circuit Court of Appeals for a writ of error and supersedeas to the judgment of the Court herein a stay of ninety days from the adjournment of the Court is granted for that purpose.

(128) In Appeal 42664 for the year 1924, the Bankers Company objects to an addition to income subject to a depletion adjustment, and arising out of receipt of a judgment against the Flanagan Coal Company. The Flanagan Coal Company owned an adjoining piece of land to our land, and we discovered they had mined across our boundary line in a particular seam of coal. I took up the question with them, and they first said they would pay for it. The matter hung fire for some months. This was in 1920 when they had gone in there, and at that time the price of coal was very high, any where from $6 to $15 a ton. They did not pay, and when I got my engineers to go down to measure the coal that had been taken out, the engineers found the Flanagan people had shot entries and we could not get in at all. I brought a suit for damages to the property, and we eventually settled it. We got $3,770 in 1924 for damage to our property, and that seam of coal, my engineers and I figured as at least $10,000, because the method of going in on that side of the hill had been absolutely destroyed. The amount so received has no relation to royalties or contract payments, and has no relation to extraction of

15,000 tons of coal or any amount. This was purely an arbitrary settlement adjustment. The statement of the deficiency letter that for income tax purposes the (129) amount of damages received has the status of royalties and that depletion is allowed on 15,000 tons estimated to have been damaged, is not correct, as we had no contracts with the Flanagan Coal Company.

CROSS EXAMINATION

The Flanagan Coal Company mined this coal I think in 1920, and we discovered they had gotten into our coal in probably two or three years afterwards. Damage suit was brought against the Flanagan Company, but we did not go to trial as it was settled before hearing between the attorneys or owners. The suit was for the recovery of value of the coal taken out, plus damages to the plant. I attended the conferences leading to the settlement, and none of us knew the amount of coal that had been taken out. We claimed damages considerably in excess of the settlement figure, but the Flanagan Coal Company at that time was in a pretty precarious financial condition, and we figured every little bit would help and get as much as we could. It appeared advisable to us to accept the settlement which they proposed. The coal mined by the Flanagan Company was subject to these lease contracts in one way, and in another way it was not. It was within the land area covered by the Vaughn Coal and Coke Company lease. The Commissioner has (130) allowed the Bankers Company a depletion upon an estimated amount of 15,000 tons of coal mined out by the Flanagan Company at the depletion rate applied by the Commissioner.

After hearing the parties on the question of the presentation of the Court record by petitioner as evidence of res adjudicata, the Board ruled:

"The Board some time ago had occasion to consider the weight to be given to the doctrine of res adjudicata. In most cases the argument for same has been made by respondent. For example, a property value as of March 1, 1913 was found in relation to the year 1917 and the taxpayer claimed the decision was based on inade-

quate evidence with the result that the Board received additional evidence and in many cases has given relief. The Courts have declared in many cases the determination of the Commissioner as to deficiencies are prima facie correct. In the instant case the District Court de-
(131) cision is most persuasive, but is certainly not decisive of the issues, and I must rule against the proposition of petitioner that it is decisive of this case. The most the Board can do concerning this Court decision and record is that it is possibly persuasive of a proper depletion rate, but is not decisive nor conclusive of same, and that is the ruling."

An exception to petitioner was subsequently granted by the Board from this ruling.

Respondent's attorney: The respondent has not rested upon this issue of depletion, and although the ruling of the Board has been anticipated to be as just given, respondent desires to back up the ruling by the record and to indicate further reasons why res adjudicata does not exist in the case of a depletion allowance, and desires to call Judge Strother as a witness for respondent.

Petitioner's attorney: The presentation of this
(132) record raises the question whether it is conclusive as res adjudicata, or merely sufficient to establish a prima facie case. As you have ruled on the issue of res adjudicata, petitioner asks your ruling whether a prima facie case is thereby established, and shifts the burden to the respondent, and probably respondent's attorney will want to be heard on that question.

Respondent's attorney: If petitioner's attorney insists on such ruling, it is only fair that you hear evidence from Judge Strother, which may be of material aid in passing on the question, and will be addressed entirely to the application of this Court decision to the pending appeals.

Judge Strother called as a witness for respondent testified as follows:

In 1913 Lease No. 1 was under contract to the Vaughn (133) Coal and Coke Company, which is still the operator under that contract so far as the Bankers Company is concerned, although the Vaughn Company subleased to the Fall River Pocahontas Colleries Company in 1916 and 1917. Lease No. 2 was operated by the Superior Pocahontas Coal Company in 1913 and is so operated at this time. In 1913 the New Pocahontas Coal Company operated Lease No. 3, and they have passed that lease along to the Monarch Smokeless Coal Company with which the Bankers Company has no contractual relation. In 1913 the Oregon Coal and Coke Company operated Lease No. 4 and was succeeded by the Solvay Colleries Company which is now known as the Kingston Pocahontas Company. The Oregon Company operated from 1909 to 1916 and the Solvay Company from 1916 to 1924, and the Kingston Company has since operated the property. Before January 1, 1923 the New Pocahontas Coal Company contract provided for a royalty per ton at 7c, and thereafter provision for 8c per ton was made. A mistake was made in the acreage at the time the contract was made, and probably 100 acres were omitted, and when it was agreed this acreage should also be operated, the rate was increased from 7c to 8c per ton. As to Lease No. 5, the original operator (134) was the Pocahontas Smokeless Coal Company, which was subsequently acquired by the New Pocahontas Coal Company, and so far as the Bankers Company is concerned, there has never been any change. When a sublessee takes over one of these properties, I do not think the original lease requires the approval of the Bankers Pocahontas Coal Company, but that question has given us considerable concern. There is no restriction in any of these contracts, and it has been assumed that the right exists to sublet without the consent of the Bankers Company. Prior to March 1, 1913 the Bankers Company had entered into so-called leases with respect to particular seams of coal. For example, the Oregon Coal Company's contract covered between 1,700 and 1,800 acres, including all seams of coal. A conditional provision of the lease required the operator to mine the coal in other seams than the one being mined at a royalty not exceeding 10c per ton, and unless such operation was begun within six months, the right might be let by

the owner to someone else. In that way, in 1916 the Kingston Pocahontas Coal Company came in and began to mine such a seam of coal. Lease No. 6 to the J. B. B. Coal Company was not operated by a different company thereafter; although the Dexcar Coal Company and (135) later the Fordson Coal Company had something to do with the lease. I assume the J. B. B. Coal Company is responsible, but the payments come from Mr. Ford, and that is entirely satisfactory at this time. The Bankers Company never approved the lease to the Fordson Company, as it was purely a stock proposition. Since 1913 there have been times when some of these lessees ran into thin coal or unminable coal, and where there were pinch-outs, or the coal could not be mined, but there has always been continuous mining of the coal.

CROSS EXAMINATION

The transactions including assignments or changes in the several lease contracts occurred in the years 1916, 1918 and 1923. The 1923 change of the contract occurred in January, and before February 17, 1923, when suit was filed in the District Court of the United States, by the Bankers Company. Since February 17, 1923, there has been no change or alterations in the terms or conditions of the old contracts, and there have been no new contracts made as to the property. The deficiency letter for 1920 issued on February 15, 1926. The deficiency letter for 1921 to 1923 inclusive issued on February 12, 1926. The deficiency letter for 1924 to 1926 in-(136) clusive, issued on January 15, 1929. The judgment in the United States Court proceeding is dated January 31, 1928, and consequently, the last deficiency letter was issued about a year after the judgment. The deficiency letter of January 15, 1929 shows a protest was made in December, 1927. A brief was filed in November, 1928 and a conference was held on December 12, 1928. In those papers and conferences reference was made to the findings of the United States District Court, which involved the years 1914 to 1919 inclusive. In the several deficiency letters, respondent used the depletion rate of .036, which was used in the tax determination for the previous years on which suit was brought. No change was made from the rate determined and applied

in the earlier years. That rate was based on a value of $510,000 by a valuation engineer, who said we had no No. 3 and No. 4 seams of coal in our property, although we were mining that coal at that time. The valuation was made by Mr. Atkinson in about 1916. The rate of .036 was a blanket rate applied to the company as a whole and to all its leases.

The parties stipulated and agreed that a rate of .036 was applied by respondent in his determination in the (137) several deficiency letters, both before and after the Court judgment.

Thereupon, petitioner moved to strike out the evidence of Strother for respondent, relating to impeachment of the Court record on the ground same cannot be impeached as an estoppel of judgment. The motion was denied and exception granted to petitioner.

The Member: Petitioner's attorney will please state the purpose for which Exhibits 1 and 2 were offered, bearing in mind the ruling that the Board will not be bound by the conclusions of the Court decision as to a proper rate for depletion.

Petitioner's attorney: Petitioner offers this judgment in evidence, and this record in evidence. The judgment is offered for the reasons I have given before, and the entire record is offered in evidence upon the issues of (138) this case insofar as applicable.

Respondent's attorney: Respondent objects on the ground that no rule of law allows a petitioner to borrow a record in some other Court of jurisdiction where the rules or the question may or may not have been the same; where the same cause of action was not involved because a different law was involved, and I see no greater force to this record than could be given by this Board to an affidavit without the parties present for examination.

The Member: The objection is overruled. The Board rules all the proof before the District Court, included in Exhibit 1, is before the Board to enable the Board to determine a proper depletion rate. Such rul-

ing does not mean the Board feels bound to accept the rate found by the Judge, and only means the competent evidence that was before the Department and included in (139) this exhibit will be considered for the purpose of determining proper depletion rates for the years in question in these proceedings. An exception is granted to the respondent and also to petitioner to so much of the ruling as states the conclusions are not considered binding upon the Board.

D. J. F. Strother, recalled for petitioner, testified as follows:

I desire to correct my previous testimony concerning cost of the Bankers property when acquired, by adding that in 1911 I made its owner a proposition and gave him a year to redeem the property. He did not make good and we took the property over at what I considered less than 50% of its value. The proposition related to some money which he owed to me and to banks with which I was connected. For this reason we did not meet from 1911 until the organization of our company in 1912.

It is stipulated the decision of the Bankers Pocahontas (140) Coal Company appeal as to the issues of coal in place, or the alternative issue of depletion value shall apply to those questions as arising in the appeals of Judge Strother.

Respondent's attorney: If the Board decides the theory of sale of coal in place is not applicable to these contracts, and the income derived from rental or royalty is subject to income taxation, its attention must turn to determination of a proper deduction from income as a depletion reserve, and to any payments of dividends out of that reserve to the stockholders, and in these respects this record fails to provide the Board with the facts on which it can determine same.

This record lacks several vital elements necessary to determination of appropriate depletion. We do not have (141) the production figure for any year, by which the rate is to be multiplied to produce the deduction; we

have no figures indicative of opinion as to how much coal was in the property; as to what would be a proper discount rate for valuation of a lessor's interest on March 1, 1913.

Upon the question of facts necessary to any computation under Rule 50 herein, the parties stipulate the following may be received, by agreement, as a statement of fact:

(Reference is made to figures shown in Board findings of fact as part hereof).

Schedule 1—Contracts of March 1, 1913—(figures omitted here because shown in Board findings of fact.)

Schedule 2—Estimated recoverable tonnage of March 1, 1913—(figures omitted here because shown in Board findings of fact.)

Schedule 3—Tonnage mined and contract payment each year—(figures for 1920 and later years omitted here because shown in Board findings of fact.)

Lease No. 1—Fall River Pocahontas Collieries Company

Year	Tonnage Mined	Paid for	Receipts
1908	986	1225	$ 98.64
1909	6152	6912	553.58
1910	25539	25537	2043.08
1911	27283	27275	2182.61
1912	20455	19525	1562.46
1913(11 months)	18404	15500	1240.62
1914(10 months)	31497	30237	2419.82
1915(10 months)	40698	71362	5709.26
1916	63048	77050	6164.67
1917	70929	69475	5558.59
1918	86025	85012	6801.99
1919	83778	83775	6702.25

Lease No. 2—Superior Pocahontas Coal Company

(143)

Blackstone Mine

Year	Tonnage Mined and Paid for	Royalty
1908	21690	$2169.03
1909	126969	12693.33
1910	93706	9370.66
1911	102033	10203.26
1912	60556	6055.60
1913	54108	5411.02
1914	47211	4721.39
1915	42804	4280.49
1916	26165	2616.54
1917	14151	1415.11

Cletus Mine

Year	Tonnage Mined	Tonnage Paid for	Royalty
1908	1606	1606	$160.62
1909	11627	11628	1162.79
1910	15802	15803	1580.33
1911	27689	27689	2768.91
1912	24169	24170	2416.97
1913	31714	31718	3171.76
1914	42088	42193	4219.27

Lease No. 2—Superior Pocahontas Coal Co. (Continued)

(144)

Cletus Mine

Year	Tonnage Mined	Tons Paid for	Royalty
1915	55469	55469	$5546.98
1916	48849	48850	4884.93
1917	49959	49960	4995.96
1918	59935	99999	9999.96
1919	55802	100000	10000.00

Lease No. 3—Pando Coal Company

Year	Tonnage Mined	Tonnage Paid for	Royalty
1908	5951	5951.	$595.13
1909	40040	40040.	4004.02
1910	34101	34103.	3410.36
1911	34044	4434.	443.44
1912	3807	15972.	1597.28
1913	-----	50818.	5081.89
1914	-----	22497.	2249.78

Note: Payments in 1912, 1913 and 1914 were made by Receivers for the Pando Coal Company. After September 16, 1912 this mine was operated by the New Pocahontas (145) Coal Company.

Atlas Coal Company

Year	Tonnage Mined	Tonnage Paid for	Royalty
1908	4139	4139.	$413.97
1909	29282	23413.	2341.33
1910	21013	1827.	182.78
1911	-----	-----	------
1912	-----	22500.	2250.00

Note: The payment of $2250.00 in 1912 was realized from sale of the property to C. C. Huffman, et al. This mine was operated by New Pocahontas Coal Company after September 16, 1912.

W. E. Deegans

Later New Pocahontas Coal Company and Monarch Smokeless Coal Company

Year	Tonnage Mined	Tonnage Paid for		Royalty
1912	1685	477.8	.07c	$349.90
1913	30558	57142.7	.07c	4000.00
1914	25974	57142.7	.07c	4000.00
1915	66144	66145.0	.07c	4630.15
1916	91538	91538	.07c	6407.66
1917	92577	127.018	.07c	8891.25
1918	135941	117.141	.07c	8891.88
1919	128770	119611	.07c	8199.88

Lease No. 4—Oregon Coal Company, Later Solvay Collieries Company and Kingston Pocahontas Coal Company.

(146) Warwick Mine—Upper Seam

Year	Tonnage Mined	Tonnage Paid for	Receipts
1908	18850	18853.	$1885.30
1909	95889	95889.	9588.98
1910	93710	93170.	9317.06
1911	107542	107542.	10754.26
1912	85885	85885.	8588.56
1913	75847	100000.	10000.00
1914	81032	100000.	10000.00
1915	73993	100000.	10000.00
1916	99418	99419.	9941.91
1917	85124	100230.	10023.00
1918	82014	100005.	10000.54
1919	75552	100000.	10000.00

Exeter Mine—Lower Seam

Year	Tonnage Mined	Tonnage Paid for	Receipts
1919	-----	75000.	$7500.00

Lease No. 5—Pocahontas Smokeless Coal Company Later
(147) Central Pocahontas Coal Co.

Year	Tonnage Mined	Tonnage Paid for	Royalty
1908 (Dec.)	3,266	3266	$163.30
1909	23,340	23340	1167.00
1910	46,592	46918	2345.90
1911	48,934	48934	2446.70
1912	52,319	52487	2624.35
1913	41,282	40722	2036.10
1914	34,067	34067	1703.35
1915	48,464	34090	2704.50
1916	60,670	54505	2725.25
1917	56,985	56981	2249.07
1918	9,133	9135	456.65
1919	-----	-----	------

Lease No. 6—Hensley Coal Company.

Later known successively as J. B. B. Coal Company, Dexcar Pocahontas Coal Company and Fordson Coal Co. The payment of 1c per ton ($300.00) minimum per year) is a haulage fee for use of an easement over Bankers Po-
(148) cahontas property to coal mined on other properties by the operators.

Year	Tonnage Mined	Tonnage Paid for	Receipts
1908	6908	6908	$69.08
1909	29950	29951	299.51
1910	43822	43825	428.25
1911	82062	86330	863.30
1912	86758	96759	967.59
1913	74950	74952	749.52
1914	98128	98129	981.29
1915	170034	169938	1699.28
1916	113647	112864	1128.64
1917	67893	67893	678.93
1918	49610	49610	496.10
1919	90729	90729	907.29

Thereupon, both petitioner and respondent rested.

Each party having tendered separate proposals of
(149) settlement under Rule 50, the following proceedings were had at a hearing before Hon. C. P. Smith, member, on June 18, 1930;

Counsel for respondent stated that the parties were in disagreement as to the methods of computing the tax; that in the respondent's computation depletion allowances were computed at the rate of 3.6c per ton upon tonnage mined each year; that this method was in accordance with the opinion of the Board in this case, and consistent with the Board's rulings in other cases, although the respondent in other cases was committed to the principle of allowing depletion on tonnage of coal paid for instead of upon tonnage of coal actually mined in a taxable year.

Counsel for petitioner stated that respondent's computations were in accordance with the Board's findings of (150) fact and opinion as they now stand but contended the Board's findings and opinion should be amended and supplemented, and the depletion allowances should be upon the basis of coal paid for.

The counter proposals for petitioner include a motion for amended and supplemental findings of fact and a reopening of the case on the grounds that the Board findings should be amended to allow depletion on coal paid for instead of upon coal mined in any year, and that the proposal of petition should be accepted as correct.

Petitioner urged a reopening was necessary because the stipulation of record and finding of the Board that a Depletion rate of 3.6c per ton was applied by respondent to all the years was evidently an error, as it appeared (151) other depletion rates were applied by respondent for the years 1924, 1925 and 1926, and both parties were in agreement as to the manifest error of the stipulation in this respect. Respondent replied that conceding said error, respondent's proposed tax computation substantially corrected same by allowance of the larger depletion rate as found by the Board to tonnage mined in the several years, and that it was thereby unnecessary to reopen the case. It further appeared a previous motion of petitioner for reopening the case and for rehearing had been overruled by the Board, without hearing. Petitioner submitted that the stipulation of tonnage mined and paid for for the several years, submitted during the hearing for purposes of any subsequent Rule 50 settlement, showed that under several leases coal paid for in several years, substantially exceeded coal mined, and offered to introduce said leases to substantiate the schedules, and to (152) show said payment was the minimum royalty required to be paid under said leases. Petitioner proffered the contents of said leases to be respectively: Lease dated January 1, 1918 to the Superior Pocahontas Coal Company; and Lease dated September 30, 1916 to the Solvay Colleries Company; each reciting the pre-existence of contracts on March 1, 1913, and the subsequent adjustment and modification of same as to payments of a minimum royalty in each year, with leave at any subse-

quent time to take out the coal therefor paid for, and whereby payments were required to be made for 120,000 tons per year—although only about 50,000 tons were actually mined in the year. Petitioner further offered to identify and incorporate each of said leases as part of the record as the best avowal of their contents and provisions.

Respondent having waived objection to the form of (153) offer, and to consideration of the contents of the leases upon the propriety of reopening the case, but having objected to the competency, relevancy and materiality of each of said leases as new matter not receivable in a rule 50 settlement. The Board sustained said objection and refused to receive said leases, and granted exceptions from its rulings thereon to the petitioner.

Thereupon, the Board further ruled:

Petitioner's argument is really directed to a rehearing or re-argument, and does not seem to me proper argument under Rule 50. If the Board is to correct its opinion and findings of fact, it must order a rehearing or re-argument, and I am very glad to get this to help us and other members in considering the argument, but I cannot accept it as anything other than a motion or argu-(154) ment for reconsideration of the case. I will receive it at this time, and if the Board is to do anything it will have to re-order a re-hearing or re-argument. The case was set down for a Rule 50 settlement, and unless the Board is to order a re-argument or a rehearing, the notice of settlement proposed by respondent must be accepted. I will consider this argument, and if the Board thinks there should be a rehearing it will order same of its own motion. I see no occasion for setting this down for further hearing under Rule 50.

Approved and ordered filed this 14th day of July, 1931.

CHARLES P. SMITH,
Member.

AGREED PRAECIPE

(155) Filed July 14, 1931.

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket Nos. 14516, 14517, 42664

Commissioner of Internal Revenue,
Respondent.

The Clerk will please include the following in the record upon the petition of appellant for review of the proceedings of the Board in the above entitled appeals (consolidated) before the United States Circuit Court of Appeals for the Fourth Circuit.

1. Docket entries, stated as follows:

(a) As to appeals 14516-14517—

"The entries in both appeals are identical and as follows:"

(Insert all entries from one appeal)

(b) As to appeal 42664—

Entries through April 27, 1929, followed by:

"After this date the entries are identical with entries in Appeals 14516, 14517 as appearing herein."

2. Petitions, deficiency letters, amended petitions and (156) answers from Appeals 14517, 14516, 42664, as follows:

(a) Docket 14517, Petition and deficiency letter (Insert) followed by Statement:

"Cletus Lease exhibit omitted because same appears in Board findings."

Answer (Insert)

Amended petition (Insert)

(b) Docket 14516 Caption, followed by statement:

"The petition, amended petition, answer and Cletus Lease Exhibit herein are identical in substance with same in Appeal 14517, as affecting adjustments and deficiencies herein contested for the calendar years 1921, 1922 and 1923, excepting as to special incidental issues removed from controversy by the subsequent Board findings and opinion, and same are therefore here omitted, excepting the deficiency letter, which is as follows:"

Deficiency letter (Insert)

(c) Docket 42664 Caption, followed by statement:

"The petition, amended petition and answer herein are identical in substance with same in Appeal 14517, as affecting adjustments and deficiencies herein contested for the calendar years 1924, 1925 and 1926, and same are therefore here omitted, excepting Paragraph (h) thereof and the deficiency letter here appearing."

Paragraph (h) of Petition (Insert).

Deficiency letter (Insert).

3. Motion granted April 30, 1929, consolidating Ap-
(157) peals 14516, 14517, 42664, for hearing.

4. Board findings and opinion.

5. Petitioner's motion for rehearing and modification, (February 27, 1930).

6. Board order denying same (March 6, 1930).

7. Respondent's Rule 50 settlement proposal (March 31, 1930).

8. Petitioner's Rule 50 counter-proposal of settlement (May 21, 1930).

9. Boards order denying motion for rehearing and reargument (July 15, 1930), and Redetermination (July 16, 1930).

10. Board order amending findings and opinion (September 26, 1930).

11. Petition for review.

12. Statement of evidence.

13. Extensions of time; orders concerning record contents, not included in record.

14. This praecipe.

(s) CAMDEN R. McATEE,
(158) Attorney for Petitioner.

Copy hereof acknowledged; all objections waived and consent record be accordingly prepared.

(Signed) C. M. CHAREST,
Attorney for Respondent.

(159) **AGREED ORDER**

United States Circuit Court of Appeals for the Fourth Circuit

Bankers Pocahontas Coal Company, Petitioner,	(B. T. A. Docket Nos. 14516
vs.	14517
Commissioner of Internal Revenue, Respondent.	42664 Consolidated).

The parties herein by their attorneys, having moved the Court for leave by agreed praecipe to establish the record herein before the United States Board of Tax Appeals to be Certified for use in this Court as required by its rule as containing the complete record as to docket entries, pleadings and other proceedings of record in one of the above entitled appeals before said Board, and to establish said record in each of the other appeals as part thereof for use in this Court, complete as to matters pertaining entirely to either of said appeals, and by reference as to matters therein which are the same in substance or in identity as in said complete record, and to consider said three appeals consolidated for hearing herein, for cause, that said three appeals before said Board involved substantially the same subject matter, (160) pleadings, proceedings and issues, and were therein heard and decided as a consolidated case and from said decision a single petition for review of said decision has been taken to this Court, and for cause that said records, if established pursuant to the rule of this Court by preparation of a single record in each Board appeals, will be repetitions, confusing and unwieldy, which the parties seek to avoid; and said parties having further moved the Court for its order to the Clerk of said Board to certify to this Court before the hearing date of said petition for review, as a supplement to said record, original Exhibits 1 and 2 of petitioner, being certified photostat copy of a certain Court record from the United States District Court of West Virginia, and it appearing a synopsis of said Court record is included in the statement of evidence, to order that the printing of said supplemental Court record be not required; and said parties having further moved the Court that, upon filing of the petition for review and record herein and in a related petition for review of D. J. F. Strother in this Court same shall proceed, together as a consolidated case under the separate captions of said proceedings for purposes of briefs, hearing and decision.

And the Court being advised in the premises, it is thereupon considered and ordered:

That *sur* single petition for review filed by petitioner (161) herein before said Board and statement of evi-

dence thereon, the parties shall file with the Clerk of said Board their agreed praecipe to establish the record herein as including the complete record in one of said appeals, as required by rule of this Court, and as including matters from the other appeals pertinent thereto, without repetition of matters appearing in said complete record but with explanatory statements of the substance and reasons for said omissions, and that said three appeals be and the same are considered consolidated and subject to one petition for review and statement of evidence for purposes of said record and hearing in this Court, and that said Clerk of the Board be and he is authorized to certify said record made as herein provided, and that any rule of this Court to the contrary is expressly waived,

And it is further ordered that the Clerk of said Board do certify to this Court before the hearing date of said petition for review, original Exhibits 1 and 2 of petitioner, being certified photostat copy of a certain Court record from the United States District Court of West Virginia, as a supplement to the record herein provided for by this order, and that printing of same be not required.

And it is further ordered that upon filing in this Court of the petition for review and record herein and in a (162) related petition for review of D. J. F. Strother, that both shall proceed together herein, but under their separate captions, for purposes of briefs, hearing and decision.

July 8th, 1931.

JOHN J. PARKER,
United States Circuit Judge.

AGREED:

(Signed) CAMDEN R. McATEE,
Attorney for Petitioner.

(Signed) C. M. CHAREST,
Attorney for Respondent.

A true copy, Teste:—

CLAUDE M. DEAN,
Clerk United States Circuit Court of Appeals
Fourth Circuit.

Bankers Pocahontas Coal Co.,
Petitioner,

(163) v. Docket Nos. 14516, 14517 and 42664.

Respondent.

CERTIFICATE

I, B. D. Gamble, Clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages 1 to 162, inclusive, contain and are a true copy of the transcript of record, papers and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 28th day of July A. D., 1931.

B. D. GAMBLE,
Clerk.

(SEAL)

PROCEEDINGS IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

No. 3215.

Bankers Pocahontas Coal Company, Petitioner.

versus

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

July 29, 1931, the transcript of record is filed and the cause docketed.

Same day, three (3) joint motions to extend the time for the settlement of evidence, and the transmission of the record to this Court are filed.

Same day, order dated February 26, 1931, and signed by John J. Parker, U. S. Circuit Judge, extending the time for a pediod of sixty (60) days from and after March 3, 1931, within which to settle statement of evidence, prepare the record and transmit same to this Court, is filed.

Same day, order dated April 22, 1931, and signed by John J. Parker, U. S. Circuit Judge, extending the time for a further period of sixty (60) days in addition to sixty days from and after March 3, 1931, granted by order of February 26, 1931, within which to settle statement of evidence, prepare the record and transmit same to this Court, is filed.

Same day, order dated June 25, 1931, and signed by John J. Parker, U. S. Circuit Judge, extending the time for a further period of thirty (30) days in addition to the time granted by orders of February 26, 1931, and April 22, 1931, within which to settle statement of evidence, prepare the record and transmit same to this Court, is filed.

Same day, agreed motion as to the record is filed.

Same day, agreed order as to the record is filed.

Memo. of Clerk: This order is printed at page 113 of the transcript of record.

Same day, the appearance of Camden R. McAtee and Wells Goodykoontz is entered for the petitioner.

August 8, 1931, the appearance of G. A. Youngquist, Assistant Attorney General, Sewall Key, Special Assistant to the Attorney General, C. M. Charest, General Counsel, Bureau of Internal Revenue, and D. M. Evans, Special Attorney, Bureau of Internal Revenue, is entered for the respondent.

September 5, 1931, twenty-five copies of the printed record are filed.

October 12, 1931, the originals of petitioner's exhibits numbers 1 and 2 are certified up to this Court.

October 17, 1931, the appearance of Andrew D. Sharpe, Special Assistant to the Attorney General, is entered for the respondent.

ARGUMENT OF CAUSE.

October 20, 1931 (October term, 1931,) cause came on to be heard, together with No. 3214, before Parker and Soper, Circuit Judges, and Baker, District Judge, and is argued by counsel and submitted.

OPINION.

Filed January 25, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS.

FOURTH CIRCUIT.

No. 3214.

D. J. F. Strother, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

No. 3215.

Bankers Pocahontas Coal Company, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

On Petitions to Review the Decisions of the United States Board of Tax Appeals.

(Argued October 20, 1931. Decided January 25, 1932.)

Before PARKER and SOPER, Circuit Judges, and BAKER, District Judge.

CAMDEN R. MCATEE and WELLS GOODYKOONTZ (MASON, SPALDING & MCATEE and GOODYKOONTZ & SLAVEN on brief) for Petitioners, and ANDREW D. SHARPE, Special Assistant to the Attorney General (G. A. YOUNGQUIST, Assistant Attorney General, SEWALL KEY, Special Assistant to the Attorney General, C. M. CHAREST, General Counsel, Bureau of Internal Revenue, and DEWITT M. EVANS, Special Attorney, Bureau of Internal Revenue, on brief) for Respondent.

SOPER, Circuit Judge:

Bankers Pocahontas Coal Company vs. *Commissioner*, No. 3215:

The subject matter of this suit involves income and profit taxes of the Bankers Pocahontas Coal Company for the calendar years 1920-1926, as determined by the Board of Tax Appeals. Deficiencies in substantial amounts were charged against the taxpayer in each of these years; and a petition to review was filed. The Board made the following findings of fact with reference to the property concerned:

"In July, 1912, the Bankers Pocahontas Coal Company, a West Virginia corporation, acquired the fee simple title to approximately 6,200 acres of coal lands, including both the surface and the mineral rights in the State of West Virginia. The land had no appreciable value except for the coal content.

Upon incorporation in 1912, the corporation acquired by formal assignment and has continued to retain the beneficial interest of the original owners in certain contracts affecting the coal content which were executed in 1901 and 1902 with various operating companies and to which contracts the 6,200 acres and coal content were subject.

These contracts were originally prepared by D. J. F. Strother, who at that time was attorney, director and stockholder in the predecessor corporations. The form

of the contracts is that prevailing in the West Virginia coal fields, which followed the Pennsylvania form of contract as introduced by Pennsylvanians who were largely instrumental in the early coal development in the West Virginia field."

Each of these contracts purported to be a contract of lease between the prior owner of the land, as lessor, and a coal mining company, as lessee, covering a tract of land in McDowell County, West Virginia, for a period of thirty years from January 1, 1901. It was provided that the lessee should have the sole and exclusive privilege of mining and coking coal on the premises, and of conducting a general mercantile business thereon. In consideration thereof, the lessee agreed to pay to the lessor, as rental for the premises, a royalty (ranging from 1c to 10c) for each ton of coal mined and sold or used for any other purpose than the manufacture of coke, and a larger amount for each ton of coke manufactured and sold upon the premises. In some cases, a minimum annual rental or royalty (ranging from $4,000 to $10,000) was agreed upon. In addition, the lessee agreed to pay all taxes assessed against the property, or the coal mined, coked or manufactured. The lessee was given the option to renew the lease at its expiration; and provision was made for the final valuation and disposition of the improvements placed upon the land by the lessee.

The contention of the taxpayer is that these contracts, executed in the years 1901 and 1902, and acquired by it in the year 1912, were sales of coal in place that were fully complete before the Sixteenth Amendment went into effect; and that the royalties received during the period 1920 to 1926 were merely payments of obligations that existed unconditionally on March 1, 1913, and were not income taxable under the federal revenue acts. It is said that this construction of mining leases as sales of coal in place is the law of the State of West Virginia, laid down by its highest court, and is therefore a rule of property which the Federal courts must respect and enforce. The Board of Tax Appeals, however, overruled this contention, and directed that the royalties should be included in the gross income of the taxpayer, subject to taxation.

The application of the income tax statutes passed in conformity with the Sixteenth Amendment to the proceeds of mining was first considered by the Supreme Court in *Stanton* vs. *Baltic Mining Co.*, 240 U. S. 103. The court held that a tax on the product of a mine is not, in its essence, a direct tax on property merely because some exhaustion of the ore body must result from the working of the mine; and that even though an adequate allowance is not made for the depletion of the mineral, the tax does not become a direct tax on property because of its ownership. On the contrary, it was held in accordance with its former ruling in *Stratton's Independence* vs. *Howbert*, 231 U. S. 399, that such a tax is a true excise levied on the business of carrying on mining operations. The Supreme Court reiterated and applied this rule in *Von Baumbach* vs. *Sargent Land Co.*, 242 U. S. 503, where it was held that royalties from mining leases on lands in Minnesota constituted income subject to the Corporation Tax Law of 1909. It was pointed out that under the law of Minnesota, such leases are not merely conveyances of the ore in place, and do not constitute a sale of any part of the land, but the ore derived from the operation of the mines constitutes rents and profits from the land. Commenting on this rule, the court said:

"Ordinarily, and as between private parties, there is no question of the duty of the federal court to follow these decisions of the Minnesota Supreme Court, as a rule of real property long established by State decisions. *Kuhn* vs. *Fairmont Coal Co.*, 215 U. S. 349, 360. Whether in considering this federal statute we should be constrained to follow the established law of the State, as contended by the Government, we do not need to determine. The decisive question in this case is whether the payments made as so-called royalties amount to income so as to bring such payments within the scope of the Corporation Tax Act of 1909. The prior decisions of this court in *Stratton's Independence* vs. *Howbert*, 231 U. S. 399, and *Stanton* vs. *Baltic Mining Co.*, 240 U. S. 103, in which the Stratton case was followed and approved, are decisive of this question."

The court also held that there was no difference as

to taxability of the gains from the mining operations, whether the ore was extracted by the mine owner, as in the Stratton case, or by a lessee of the owner, as in the case of the Sargent Land Company.

All of this ground was considered by the Circuit Court of Appeals of the Third Circuit in *Rosenberger* vs. *McCaughn*, 25 F. (2d) 699, a case which related to income taxes based on royalties or rents from coal lands in Pennsylvania. In that State, the courts apply a different rule from that in vogue in Minnesota, and hold that mining leases constitute sales of the mineral in place; and it was therefore argued that the case must be distinguished from the decisions of the Supreme Court we have cited. But it was held, and we think properly, that the rules of decision laid down by the state courts with regard to property, while generally controlling upon the federal courts, do not necessarily govern those courts in the interpretation of the laws of Congress in regard to taxation and, it was pointed out that in *Von Baumbach* vs. *Sargent Land Company, supra*, the Supreme Court had reached the conclusion that royalties from mines constituted taxable income wholly aside from the construction placed by the Minnesota courts upon mining leases. The Supreme Court declined to review this interpretation of its decision when it denied *certiorari*, 278 U. S. 604. See also *Hirschi* vs. *United States*, 67 Ct. Claims 637, *certiorari* denied 280 U. S. 576; *Berg* vs. *Commissioner*, 33 F. (2d) 641, *certiorari* denied 280 U. S. 598; *Burkett* vs. *Commissioner*, 31 F. (2d) 667, *certiorari* denied 280 U. S. 565; *Alexander* vs. *King*, 46 F. (2d) 235.

We shall assume, for the purposes of this decision, that the law of West Virginia, like that of Pennsylvania, is that a mining lease constitutes a sale of the mineral in place. It was said in *Coal Company* vs. *Overholt*, 81 W. Va. 427, 434, that the English and many American decisions hold that when, in a mining lease, the parties contract with reference to a mineral known to exist, the quantity of which is unknown and incapable of exact ascertainment, and the lessee covenants to bring forth a minimum quantity annually, and to pay a minimum royalty, the contract amounts to a sale of the mineral in the land and the lessee is bound to pay the minimum price. See also *Feather* vs. *Baird*, 85 W. Va. 267; *Urp-*

man vs. *Lowther Oil Co.*, 53 W. Va. 501; *Toothman* vs. *Courtney*, 62 W. Va. 167; *Smith* vs. *Root*, 66 W. Va. 633.

Nevertheless, we think that the royalties in question, subject to the deduction allowed by the Acts of Congress, constitute taxable income. There can be no doubt that it was the intention of Congress to tax them. It is provided in Section 234a of each of the pertinent statutes, to-wit, the Revenue Act of 1918, 40 Stat. 1057, the Revenue Act of 1921, 42 Stat. 227, the Revenue Act of 1924, 43 Stat. 253, and the Revenue Act of 1926, 44 Stat. 9, that in computing the net income of a corporation subject to the income tax, in the case of mines and other natural deposits, there shall be allowed as a deduction, a reasonable allowance for depletion, according to the peculiar conditions in each case. It does not follow, as the taxpayer assumes, that the royalties cease to be income under the Acts of Congress because the leases are sales and the royalties are part payment of the purchase price under the law of West Virginia. It is obvious, as the Supreme Court has pointed out, that something more is involved under a mining lease than a sale and delivery of valuable property. Before the business is complete, there must take place the whole process of locating, extracting and preparing the ore for market. This is a manufacturing process, and in this aspect the royalties are seen to be income of the business and as such, subject to taxation. The federal courts must respect the local laws of property laid down by the courts of the state, but the power of Congress to tax must be judged by the realties of the situation and not by the logic of state rules of property, pushed inexorably to their extreme.

In *Weiss* vs. *Wiener*, 279 U. S. 333, the taxpayer, who was in the business of taking long leases on real property and subletting, claimed the right to make an annual deduction from his income for estimated depreciation of the buildings, but the Supreme Court decided that the claim was unfounded since he was not the owner of the property. The court said (p. 337):

"It does not matter that in Ohio, where the properties lie, these long leases are treated as in many respects like conveyances of the fee. The Act of Congress has its own criteria, irrespective of local law, that look to certain rather severe tests of liability and exemption

and that do not allow the deductions demanded whatever the lessees may be called. We understand this to be the view taken by the Department for a long time, and we are of opinion that it should not be disturbed."

It may be noted, in passing, that the Supreme Court of Appeals of West Virginia itself did not apply the rule with regard to mining leases literally when it came to the subject of taxation; for in *Harvey Coal & Coke Co.* vs. *Dillon*, 59 W. Va. 605, it held that a mining lease, similar in all substantial respects to those involved in the pending case, constituted a chattel real, taxable to the lessee under a West Virginia statute which provided for the taxation of personal property, including, in that term, chattels real. This decision was made notwithstanding the contention that the deed created not a chattel real but a sale of the coal itself *in situ*, taxable only as realty.

The taxpayer does not seem to deny the force and effect of the decisions of the Supreme Court we have cited, but claims that the Court has since discarded the theory laid down in these cases and has returned to the well established rule that the state law of property must be accepted and applied by the federal courts. Reference is made to *Tyler, Adm.* vs. *United States*, 281 U. S. 497, *Crooks, Col.* vs. *Harrelson*, 282 U. S. 55, and *Poe, Collector* vs. *Seaborne*, 282 U. S. 101; but it is obvious that each of these decisions turned upon the fundamental question whether the property sought to be taxed came within the purview of the taxing statutes. When it was clear that such was the case, the federal statute was given effect; as in *Tyler* vs. *U. S.*, 281 U. S. 497, where the court held that the value of a tenancy by the entireties should be included in the gross estate of a decedent, for the purpose of computing the tax upon the transfer of the net estate, although, under the state law applicable to such an interest, it could not be said in a strict sense of the term that a transfer of the property had taken place. In the other cited cases, on the other hand, property was held to be excluded from the tax proposed because it did not come within the terms of the statute, and this conclusion was maintained although it was occasioned by observance of a state rule of property, and it was clear that the ruling would bring about a lack of uniformity in the incidence and operation of the tax in

different states by reason of diversity of local property rules. The Supreme Court has never abandoned the rule as to the effect of state decisions on questions of property; but it has held in some instances that state decisions do not cover the whole ground to which the federal taxing statutes relate, and in other instances, that the statutes or decisions of the state lay down rules which define and limit the property which Congress has undertaken to tax.

It is next objected that even if the royalties of the mine are taxable, an insufficient allowance for depletion has been made. The Commissioner estimated the allowance at 3.6c per ton, as the value of the coal in place on the basic date of March 1, 1913; and the deficiencies were determined on this basis. The taxpayer contends that an allowance of 5c per ton should have been made because this sum has been fixed as *res adjudicata* between the parties by reason of a judgment of the District Court of the United States for the Southern District of West Virginia rendered on January 21, 1928. The Commissioner had previously determined a deficiency against the taxpayer for the years 1914 to 1919, using the unit value of 3c per ton, and had imposed additional taxes in the sum of $6,267.08, which the corporation had paid under protest. Thereafter it brought an action against the Collector of Internal Revenue at Parkersburg, West Virginia, wherein the court determined that the rate should be 5c per ton, and rendered a judgment in favor of the taxpayer for $5,373.01, which the United States paid. Hence the taxpayer claims that the question is no longer open between it and the government, since it is a general principle that when a fact is distinctly put in issue, and directly determined by a court of competent jurisdiction between the parties in a law suit as a ground for recovery, it cannot be disputed in a subsequent suit between the same parties or their privies, even if the second suit is for a different cause of action. *Southern Pacific R. R.* vs. *U. S.*, 168 U. S. 1, 48; *New Orleans* vs. *Citizens Bank*, 167 U. S. 371.

The rule is applicable, however, only when the subsequent suit is between the same parties or their privies. The taxpayer maintains that we have that situation in the present litigation because the United States in reality is its opponent in both cases, being represented by the

Collector of Internal Revenue in the prior suit, and by the Commissioner of Internal Revenue now. But the argument is refuted by the decision in *Sage* vs. *United States*, 250 U. S. 33, where it was expressly ruled, against the protest of the government, that the court was not bound by a judgment in a former suit concerning the same subject matter between the taxpayer and a Collector of Internal Revenue, because a suit against a Collector of Internal Revenue is personal and its incidents, such as the nature of the defenses open and the allowance of interest, are different. This ruling has recently been cited with approval by the Supreme Court in *Graham & Foster* vs. *Goodcell*, 282 U. S. 409, 430. The decision of the District Court for the Southern District of West Virginia was therefore not binding upon the Commissioner, and he had the authority to determine anew, as a question of fact, what allowance should be made for the depletion of the mine.

In reviewing the Commissioner's determination, the Board took into consideration not only the evidence introduced before the District Court in the prior case, but also additional evidence. The president of the corporation testified that the cost of the property, when acquired in 1912, did not exceed $507,000, a fact casting strong light on the value of the property on March 1st of the following year; in 1915, an engineer estimated that there were then twenty million tons of mineable coal, having a total value of one million dollars; on December 31, 1917, an entry was made upon the general ledger of the taxpayer that the estimated value as of March 1, 1913, on the basis of twenty million tons of coal at 5c a ton was one million dollars; and the income tax return filed for these years claimed a March 1, 1913, value of the property of one million dollars. A stipulation, filed by the parties before the findings of fact and opinion of the Board were made, to be received as a statement of fact upon any question necessary to any computation under Rule 50 of the Board, contained a schedule showing that the estimated recoverable tonnage on March 1, 1913, was 37,608,642 tons. The stipulation also included a resume of the leases, with the approximate acreage and royalties per ton in each, and also the tonnage mined and royalties received for the years 1913 to 1919 inclusive, as well as the tonnage mined, the tonnage paid for and

the royalties received for the years 1920 to 1926. From this resume of facts, it is obvious that there was substantial evidence to support the finding of the Board. As it pointed out, an allowance of 3.6c per ton would return to the taxpayer a total of $1,353,911.11 upon the tonnage estimated in the stipulation. It is true, as the taxpayer contends, that a different result might have been based upon the evidence in the record; but it is not the province of this court to find the facts anew. We merely ascertained whether there is substantial evidence to support the findings of the Board.

The taxpayer objects to the use by the Board, in determining the depletion rate, of the estimated tonnage in place on March 1, 1913, as shown by the stipulation. It is said that the stipulation was made merely to aid in the computation of the deficiency under Rule 50. The rule is applicable when the Board determines the issues in any proceeding, and withholds decisions of deficiencies for later computation. If the parties are in agreement as to the amount, copies of their computation are filed for entry of the decision; but if not in agreement, the parties may file their respective computations, and an opportunity to be heard is afforded. But any hearing is strictly confined to the consideration of the correct computation, and no argument may be made upon issues or matters disposed of by the report of the Board, or upon any new issues. The stipulation was filed in this case before the time had arrived for the filing of computations under the rule. The Board had not yet determined the principles to be applied in the computation of the deficiencies, and one of the important issues was the rate of depletion to be used in case the royalties should be held to be income. The stipulations of fact were obviously filed by the parties to enable the Board to reach correct conclusions upon the disputed points. We think the Board properly took the stipulated facts into consideration in determining the depletion allowance. They could not justly have been considered for one purpose, and not for others.

After the Board had filed its findings and opinion, the parties filed conflicting computations of deficiency, which then came on for hearing under Rule 50. The taxpayer then for the first time made the point that the schedules filed showed that under two leases, the coal

paid for in several years substantially exceeded the coal mined, and offered to introduce the leases to show that the payments were made as minimum royalties required under the contracts, with leave, to the lessees, at any subsequent time, to take out the coal paid for. The Commission objected to the offer as new matter not receivable at that stage of the proceedings, under the provisions of the rule. The Board decided that the offer constituted in effect a request for rehearing and reargument; and finally filed its order of decision without granting a rehearing or considering the evidence offered. This ruling the taxpayer assigns as error.

It is provided in Regulations 45, 62, 65 and 69, Article 216, that in case a lessee under a mining lease is required to pay annually a specified sum to be applied in payment of royalty for mineral, whenever the same shall be extracted and removed, the value in the ground to the lessor, for purposes of depletion, of the number of units so paid for in advance, will constitute an allowable deduction from the gross income of the year in which the payment shall be made. It would have been proper to have introduced the leases in evidence at the original hearing of the case before the Board had determined the issues involved. But the taxpayer put in evidence only one of the contracts of lease as typical of all the rest. Under this form of lease, the right of the lessee to mine additional coal to offset the excess of royalty paid in any year was limited to the next succeeding year after the amount necessary to produce the minimum royalty for that year had been mined. To such a situation under the facts proved, Article 216 had no relevance. The Board was accordingly correct in its ruling that to receive in evidence the new matter offered by the taxpayer was equivalent to the granting of a rehearing of the case. It was within the sound discretion of the Board to grant or deny the taxpayer's motion; and since the evidence must have been in the possession of the taxpayer from the beginning, we cannot say that the discretion of the Board was abused. *Boggs and Buhl* vs. *Com.*, 34 F. (2d) 859, 861.

Another question for decision relates to the sum of $3,770.40 paid to the corporation in 1924 as damages for an unlawful trespass. The Board made the finding of fact that in 1920, the Flanigan Coal Company, which

owned land adjacent to that of the taxpayer, trespassed on the latter's land and removed coal to which it had no right. It then destroyed the entries and as a result the extent of its operations could not be determined. The situation was discovered in 1923, whereupon the taxpayer brought suit for damages and claimed compensation not only for the coal removed, but also for damages to the property. In 1924 the suit was compromised by the payment mentioned, but this settlement had no relation to the coal extracted as the amount of the same could not be determined. The Board quoted the testimony of the president of the corporation to the effect that the destruction of the entries had absolutely destroyed the method of going into the mine at that point; that he and his engineers had estimated that the damages to the property and to the seam of coal were at least ten thousand dollars; and that $3,770.40 was accepted because the trespasser at the time was in a precarious financial condition.

The Commissioner held that the damages received constituted gross income in the year 1924; that the trespasser had mined or damaged 15,000 tons of coal; and that the taxpayer was entitled to deduct from the amount received the sum of 3.6c per ton, or $540, for depletion. The Board sustained this action. It said that a loss caused by a tortious act, if not compensated for by insurance or otherwise, is deductible from gross income; but that the evidence did not afford facts from which the amount of the loss might be determined; and that the cost of the coal removed by the trespasser or its value on March 1, 1913, was not known. Hence it held that no deduction could be allowed for loss in 1920. As to the year 1924, it made the following statement:

"The same situation obtains with respect to the year 1924. The company received from the trespasser $3,770.40. The petitioner has found that all but $540 of this amount (which he has allowed as a deduction from gross income as depletion) constituted taxable income of the company for 1924. The company has submitted no evidence that the cost or March 1, 1913, value of the coal removed by the trespasser was in excess of $540 or that such basis plus damages to the property was in excess of $540. The determination of the Commissioner

is therefore sustained for lack of evidence showing error on the part of the respondent."

The taxpayer objects to this addition to its income for the year 1924, on the ground that the money paid by the trespasser was merely compensation for injury to the mine, and was in effect a return of capital. Any loss or gain in the transaction could be determined under the circumstances only upon a final disposition of the property. We think this position is sound. If the taxpayer were asking for a deduction from income in 1920 for the loss caused by the trespass in that year, it would be within the province of the Board to determine whether the evidence submitted by the taxpayer was sufficiently definite to justify the allowance claimed. The finding of the Board, that the amount of the coal removed could not be ascertained, showed that the amount of the loss was uncertain. But this finding likewise shows that the Commissioner's action in adding the sum of $3,770.40 to the gross income of the taxpayer in 1924, was without foundation. If there had been substantial evidence to support the finding that 15,000 tons of coal had been unlawfully extracted, and that $3,770.40 had been paid solely in settlement of that wrong, it would have been proper to have added this amount to the gross income, less the expenses for collection and an allowance for depletion. The balance remaining would have been as clearly profit in the taxpayer's hands as if it had been paid by a lessee operating on a royalty basis. But the situation is confused by the fact that the amount of coal extracted is not known. So far as can be told from the record, the amount paid by the trespasser may not have exceeded payment at the rate of 3.5c per ton. In addition, there is the uncontradicted evidence of substantial damage to the approach to the mine.

These circumstances show that the Commissioner was not warranted in adding the sum of $3,770.40, less an estimated depletion allowance of $540 to the corporation's taxable income for the year 1924. We are not dealing with a situation like that considered by the Supreme Court in *Burnet* vs. *Sanford & Brooks Co.*, 282 U. S. 389, but with a loss of capital investment. In *Doyle* vs. *Mitchell*, 2447 U. S. 179, 185, the court, speaking of such a question, said: "In order to determine whether

there has been a gain or loss, and the amount of gain, if any, we must withdraw from the gross proceeds an amount sufficient to restore the capital value that existed at the commencement of the period under consideration." A taxpayer is not allowed to deduct a loss from gross income until the amount is definitely fixed and ascertained; and for the same reason, he should not be charged with gain on pure conjecture unsupported by any foundation of ascertainable fact. See *Burnet* vs. *Logan*, 283 U. S. 404.

It follows that as to the determination of the deficiencies of the corporation for all of the years in question except the year 1924, the action of the Board is affirmed, and as to that year, the case is remanded for further proceedings in accordance with this opinion.

Strother, Petitioner, vs. *Commissioner of Internal Revenue,* No. 3214.

This case relates to the income of a stockholder of the Bankers Pocahontas Coal Company derived from dividends by which the greater part of the royalties which the corporation received, were distributed. During the several years involved in the foregoing case, 1920 to 1926, Strother, as one of the corporation's stockholders, received dividend payments from the company and reported them in his income tax returns, but did not return them as taxable income. The Board found, in its original findings of fact, that the corporation made distribution of the entire amounts received by it as royalties, including any depletion reserve. The Commissioner determined as deficiencies against Strother the total amounts received by him from the company, and made no allowance for that part of the moneys which constituted depletion of the capital. Upon these facts, the Board held in its opinion that to the extent that the distribution made by the corporation constituted a distribution of depletion reserve, the amount received by Strother was non-taxable.

The opinion established, as we have seen, that the royalties constituted income to the corporation, and not the proceeds of sale of mineral in place, and that the proper allowance for a depletion reserve was at the rate

of 3.6c per ton. By stipulation of the parties, the decision on these matters was adopted in the Strother case. After the decision was rendered, a hearing was held upon the recomputation of the Strother deficiencies. Strother objected to the new computation proposed by the Commissioner because it did not provide for the deduction from the dividends received of a proportionate part of the entire allowance for depletion. It seems that the total depletion allowance of the corporation for the years in question was $125,000, but the computation was made as if the total allowance was only $90,000. Apparently, the Commissioner held that a sum retained by the corporation in each year to meet the tax deficiency, was in fact part of the allowance for depletion, and to that extent, the allowance for depletion had not been included in the dividends. Another question seemingly involved was whether or not in determining how much of the dividends were capital, the total net income and the total depletion for the year should be pro rated to the date of each dividend payment.

These questions appear to be those which are raised by the petitioner; but the record in the case is so vague that we cannot obtain a clear conception either of the facts to be considered or the questions of law to be decided. This situation doubtless arose because the important questions in which the parties were interested were those concerning the character of the royalty payments as return of capital or income, and if income, the proper allowance to be made on account of depletion. A decision could not be reached in the Strother case until these questions had been determined. At the hearing on the question of recomputation of the Strother deficiencies, it was pointed out by counsel for the Commissioner that the record did not supply a complete basis for recomputing the Strother tax; that, strictly speaking, the taxpayer had failed to maintain the complete burden of proof, but that this was not reasonably to be expected under the circumstances. It was conceded that the recomputation proposed by counsel for Strother was literally in compliance with the decision of the Board, but that this decision was in need of revision. Thereupon, the Board announced that it would make an amendment of its findings of fact, and this was filed after the hearing. Instead of the statement that the corporation distributed

the entire amount received from its operating contracts, the finding was substituted that the corporation used such portion of the royalties as was necessary for the payment of administration expenses, set aside a certain reserve to meet the federal taxes, and distributed the rest to the stockholders. No change was made in the opinion as to the holding that to the extent the amounts received by Strother included depletion reserve, they were not taxable; and without further recomputation, the decision complained of was promptly entered.

The government's brief in the case before us suggests that the record does not contain sufficient facts to permit a determination of the questions raised, and that therefore the Board's decision should not be disturbed. We think, however, that under the circumstances, it would be just for the Board to give further consideration to the Strother case, and to afford to the taxpayer an opportunity to introduce additional testimony to bring out the facts necessary to a decision of the issues involved. The case will therefore be remanded for further proceedings in accordance with the opinion in the case of *Bankers Pocahontas Coal Company* vs. *Commissioner*, insofar as it determines the questions involved herein, and without prejudice to the right of petitioner to rely upon the legal positions as to other matters urged upon this appeal.

Case No. 3214, *Remanded for further proceedings.*
Case No. 3215, *Modified.*

JUDGMENT.

Filed and Entered January 27, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS,

FOURTH CIRCUIT.

No. 3215.

Bankers Pocahontas Coal Company, Petitioner.

vs.

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

This Cause came on to be heard on the transcript of the record from the United States Board of Tax Appeals, and was argued by counsel.

On Consideration Whereof, It is now here ordered and adjudged by this Court that the decision of the said Board of Tax Appeals, in this cause, be, and the same is hereby, affirmed except as to the determination of the deficiencies of the corporation for the year 1924, and as to this year, this cause be, and the same is hereby, remanded to the United States Board of Tax Appeals for further

proceedings in accordance with the opinion of the Court filed herein.

January 27, 1932.

MORRIS A. SOPER,
U. S. Circuit Judge.

February 8, 1932, petition of petitioner for a stay of the mandate is filed.

Same day, order staying mandate is filed.

PETITION OF PETITIONER FOR A REHEARING.

Presented February 26, 1932.

United States Circuit Court of Appeals for the Fourth Circuit

No. 3214

D. J. F. STROTHER, PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

No. 3215

BANKERS POCAHONTAS COAL COMPANY, PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

PETITION FOR REARGUMENT AND REHEARING BY EACH PETITIONER.

Come the petitioners herein by their attorneys, and move the Court for a reargument of the cases pre-

sented, and a rehearing of the Court's decision of January 25, 1932, particularly for the reasons and causes herein specifically stated, as well as others apparent on the records, and to be amplified by reargument and rehearing.

The respondent taxgatherer proposes to assess and levy the taxes in controversy solely as taxes upon income authorized by the XVI Amendment, and imposed under the several Revenue Acts which give effect to said Amendment.

The petitioning taxpayers herein protest against said assessment and levy on the ground that said income taxes are neither authorized by the XVI Amendment, nor imposed by the various Revenue Acts.

A citizen may owe a tax as of right, but under the law he may not owe same. In case of doubt whether a tax is owing, the citizen may claim the benefit of the doubt.

In support of the present motion, petitioners respectfully would show the Court has erred as follows (error indicated by black face type):

(1) This Court holds:

> The certain instruments executed in 1901 by a land-owner (whose resulting interest was acquired by petitioner corporation in 1912), granting the exclusive right to mine the coal-content from said land until exhausted in consideration of payment by the grantee of a fixed amount per ton mined each year, and of a fixed minimum annual payment, effected sales of coal in place under the Laws of West Virginia where the lands are situate; **that the payments receivable by the grantor (or its assignee) pursuant to said instruments in the several years, are royalties,**

which Congress intended to subject to income tax under the several Revenue Acts enacted pursuant to the XVI Amendment after deduction therefrom of the depletion allowances provided by said Acts as available to a lessor.

The definite errors are:

(a) By said sale in place, as effected before the enactment of the XVI Amendment on March 1, 1913, was created the right to recover or collect the purchase money in the ensuing years before and after said date, and said payments, whether called royalties or not, when received after said basic date are not taxable income in whole or in part.

(b) The Congress has only allowed depletion to the owner of an interest in the depletable property, including lessor and lessee, and has not allowed nor intended to allow depletion to a vendor who has parted with interest in the property.

(c) The Revenue Acts make other provisions for determination of the taxable profit of a vendor.

(d) This Court has wrongly applied the law to the facts of the case.

(2) This Court holds:

That the depletion rate of 3.6 cents per ton is applicable to coal mined, and not to coal paid for but not mined, whereby the payments, as to the excess of any payment over the part thereof determined by the quantity of coal mined, is not subject to any depletion allowance.

The error is:

(a) The depletion unit, being premised upon the expectancy of entire annual minimum pay-

ments, should apply to coal paid for instead of coal mined in the several years.

(b) The Courts have reversed the position of the Board as herein substantially adopted by this Court.

ARGUMENT.

These points of decision are argued here because if the error alleged in the first be admitted, the second is immaterial. In presenting the cases, the parties were in conflict as to the construction of the instruments under the West Virginia precedents, petitioner contending they effected sales in place, and respondent contending they were only leases. The parties were not in conflict that the West Virginia rule, whatever the Court found it to be, was decisive of the liability of the payments to tax. In view of the uncertainty whether a sale in place was effected, petitioners before the Board and before this Court, were obliged to argue the sufficiency of the depletion allowance as the alternative arising for decision if there was no sale in place. When a sale in place is established the amount of depletion becomes immaterial, as that issue is removed from the case. The vendor who has parted with the depreciable property can have no depletion allowance against its sales proceeds, under the Revenue Acts.

Now, that this Court specifically holds the instruments effected sales of coal in place, the path is straightened toward final and correct determination of the rights of the parties under the XVI Amendment and several Revenue Acts. In addition to the grounds given in the opinion for holding a sale in

place was effected, specific reference to the instruments strengthens said conclusion. It appears, that the vendor owner covenants the purchaser of the coal content *"shall have quiet and peaceful enjoyment of same"* (the certain tract of land), thus giving the purchaser *control* and *possession* of the whole tract; the vendor owner further gives the purchaser *"the privilege* of using so much of the surface of said land, and so much of the lumber, stone, sand, clay and water *as may be necessary"*, thus evidencing the intent of making a severance of realty, and giving entire possession for benefit of the purchaser from any, dominion, control or possession by the vendor owner. The interpretation of these unique and unusual provisions is controlled by the manifest intentions of the parties, and is but little influenced by other contracts of a like general nature, but lacking such direct contractual provisions, and leads inevitably to the conclusion that a sale in place was intended and effected.

This brings us to the discussion of the specific errors above alleged:

1(a) By said sale in place, as effected before the enactment of the XVI Amendment on March 1, 1913, was created the right to recover or collect the purchase money in the ensuing years before and after said date, and said payments whether called royalties or not, when received after said basic date were no more taxable income than were the payments of same received before said date.

The XVI Amendment, says Mr. Chief Justice White in *Stanton v. Baltic Mining Co.*, 240 U. S. 103:

"conferred no new power of taxation"—

In his earlier opinion in *Brushaber v. Union P. R. Co.*, 240 U. S. 1, Judge White pointed out that Congress was invested by the Constitution with every conceivable power of taxation, subject to provisions thereof that direct taxes should be apportioned and indirect taxes should be uniform, and that the income taxes of the Civil War were classed as indirect taxes.

The opinion explains the XVI Amendment became necessary to remove the principle enunciated in the *Pollock* case (157 U. S. 429), that a tax upon income enacted as an excise tax subject to the rule of uniformity was a charge upon invested property, and, to that extent, was a direct tax requiring apportionment, and consequently unconstitutional.

In *Evans v. Gore*, 253 U. S. 245, the genesis of the XVI Amendment is reviewed, together with intervening precedents, as a basis for conclusion that same did not extend the taxing power to new or excepted subjects. Reference is made in the opinion to the message of Governor Hughes to the New York Legislature, expressing the fear that same might extend to excepted subjects, and to the assurances to the contrary thereby obtained.

As the XVI Amendment does not add to the power of Congress to tax, and merely struck down the *Pollock* principle, as said in the *Baltic Mining* case in that it

> —"simply prohibited the previous complete and plenary power of income taxation possessed by Congress from the beginning from being

> taken out of the category of indirect taxation to which it inherently belonged, and being placed in the category of direct taxation subject to apportionment by a consideration of the sources from which the income was derived''—

it follows the XVI Amendment authorizes no income tax upon a claim accrued before and existing on March 1, 1913, when subsequently recovered or collected. The proposition states itself and is a mirror for our argument. Such a claim was capital, and the realization of its subsequent proceeds remains as capital. Thus in *Burnet v. Logan,* 283 U. S. 404, taxpayer after March 1, 1913, sold certain stock for a consideration payable in cash and in the receipt of certain royalties upon ore subsequently mined. It is held she received no taxable income in the payment to her of the royalties, until and after such payments had returned to her the value of her stock when same was sold, and that any attempt to state a partial capital return by depletion calculations would be and is a determination of income by mere conjecture not available to respondent, and not to be imposed on taxpayer.

In the present case for example, the receipts including the years in controversy since March 1, 1913, total $750,000 which is less than the $1,000,000 value in 1913 which the Board and Court says will be returned to the extent of $1,300,000 upon exhaustion of the mines. It follows said capital value of 1913 has not been received, and that no income is contained in the annual payments. If there be no income, the entire receipt is a return of capital.

Test it as you will, the annual receipt of payments of the purchase price for the sale of coal in place is the return merely of capital without income increment.

1(b) The Congress has only allowed depletion to the owner of an interest in the depletable property, including lessor and lessee, and has not allowed nor intended to allow depletion to a vendor who has parted with interest in the property.

If this proposition is correct, it is not necessary to argue for the weight that Congress may or may not give to state rules of property in levying the income tax. That Congress must and does recognize the state rules of property becomes self-evident.

In *Stanton v. Baltic Mining Co.*, 240 U. S. 103, and *Burnet, Commissioner, v. Thompson Oil and Gas Co.*, 283 U. S. 301, the rule is definitely stated that a taxpayer is not entitled as a matter of right to make any deduction from annual income for depletion, and authority therefor must be found in the Revenue Acts. The several Revenue Acts allow the prescribed deduction to an owner, and to lessor and lessee, by equitable apportionment of same between them. The deduction is not allowed otherwise, and the right to it is strictly construed. Thus the *Thompson Oil* decision denies any increase in the depletion deductions for later years to redress the apparent inadequacy of deductions previously permitted. In *Darby Lynde Co. v. Commissioner*, 51 F. (2) 32 (C. C. A. 10) (cert. denied, 52 S. C. 40), the depletion on discovery value available to a partnership is denied to a successor corporation created and owned by the partners. In *Pugh v. Commissioner*, 49 F. (2) 76 (C. C. A. 5) (cert. denied, 52 S. C. 22), the taxpayer is held upon conveyance by him of his interest in a mineral lease to thereby lose

the right to depletion as to said interest, the ground being he has become a lessee without investment. In *South Vernon Oil Co. v. Hopkins,* 49 F. (2) 1028 (C. C. A. 5), the conclusion is the same, notwithstanding the Revenue Act of 1926 defines allowable depletion as a fixed per cent of gross income from the property during the taxable year, on the ground the sale severed the depletable interest in the property. In *Fleming v. Commissioner,* 6 B. T. A. 900, affirmed 50 F. (2) 1075 (C. C. A. 9), the life beneficiaries under trusts are held not entitled to depletion against trust income consisting of royalties from ore properties. In *Murphy Oil Co. v. Burnet, Commissioner,* — F. (2) — (January 11, 1932) (C. C. A. 9), the Court describes the statute:

> "The Statute with reference to depletion of oil properties is a special one with reference to the particular subject of oil leases involving the production of oil and minerals from mines, and the consequent return of capital by the owners of interests therein, and controls over other general provisions of the law in regard to the return of capital investments."

In *Weiss v. Wiener,* 279 U. S. 333, as this Court says: The depreciation upon buildings contended for by taxpayer was disallowed notwithstanding his long lease savored of a fee under the laws of Ohio, because:

> "The Act of Congress has its own criteria, irrespective of local law, that look to certain rather severe tests of liability and exemption and that do not allow the deductions demanded whatever the leases may be called"—

which is a reiteration of the fact of the case, stated in the opinion as follows:

> —"he must show an interest in the property and a present loss to make the statute apply."

Mr. Justice Holmes correctly finds Wiener as lessor was merely renting the property and improvements, and being without interest therein, had no right to the depreciation allowance prescribed in the Revenue Act. In so doing, reference is made to *Lynch v. Allworth Stevens Co.*, 267 U. S. 364, where a lessee is declared entitled to depletion, although without title to the ore deposit, since the right to remove the ore is a property right which decreases as the mine is exhausted. There is no decision that the so-called lessor remains a lessor after parting with title to the mineral. We do not believe this Court intended to lay down that unique proposition of law in its opinion, but such is its effect.

Admitting the "Act of Congress has its own *criteria*, irrespective of local laws", it appears *interest in the depreciable or depletable property* is part thereof, and that in case of severance of the interest, or failure to acquire the interest, the taxpayer has no right to depreciation or depletion. But the Act of Congress does not prescribe the *criteria* of severance, and same must be found in the local law. If the discoverer of mineral conveys same he loses his right to depletion, and his purchaser does not acquire the right to deplete upon a discovery value. If the lessor sells his royalty interest, or the lessee sells his contract interest, each loses the right to depletion. If an owner sells coal in place, the right to depletion passes

to the purchaser and cannot be forced upon the vendor by the decision of this Court when not authorized by the Revenue Acts.

That the *criteria* of severance is derived from the local law appears in *Group One Oil Corporation*, 283 U. S. 279, where the local law of sale of mineral in place was held to divest the property of its previous immunity from tax. We point out other instances hereafter.

We have said it was not necessary to argue the weight to be given to local laws of property by Congress to sustain the present proposition. We are here dealing with real property and the position of Congress and of the Courts is that such rules must be recognized and given effect.

In *McCormick v. Sullivant*, 10 Wheat. 192, we read:

> "It is an acknowledged principle of law, that the title and disposition of real property is exclusively subject to the laws of the country where it is situated, which alone can prescribe the mode by which a title to it can pass from one person to another."

In *United States v. Fox*, 4 Otto 315, we read:

> "The power of the State to regulate the tenure of real property within her limits, and the modes of its acquisition and transfer, and the rules of its descent, and the extent to which a testamentary disposition of it may be exercised by its owners, is undoubted. It is an established principle of law, everywhere recognized, arising from the necessity of the case, that the disposition of immovable property, whether by deed, descent or any other mode, is exclusively subject to the government within

> whose jurisdiction the property is situated. *McCormick v. Sullivant,* 10 Wheat. 202. The power of the State in this respect follows from her sovereignty within her limits, as to all matters over which jurisdiction has not been expressly or by necessary implication transferred to the Federal Government. The title and modes of disposition of real property within the State, whether *inter vivos* or testamentary, are not matters placed under the control of Federal authority. Such control would be foreign to the purposes for which the Federal Government was created, and would seriously embarrass the landed interests of the State."

As the sale in place made the owner and corporate petitioner (its successor), a vendor, Congress, through income tax taxation or otherwise, could not treat such vendor as a lessor. The proceeds of the sale in place became purchase money not rentals under a lease, and they so remain. If A owned no property he is not taxable as an owner, vendor or lessor, or if he leased his property he is not taxable as a vendor, or if he sold it he is not taxable as a lessor. As said in *Nichols v. Coolidge,* 274 U. S. 531:

> "—under the mere guise of reaching something within its powers, Congress may not lay a charge upon what is beyond them. Taxes are very real things and statutes imposing them are estimated by practical results."

1(c) The Revenue Acts make other provisions for determination of the taxable profit of a vendor.

Only a few pertinent decisions are given in support of this proposition for the sake of brevity. In *Fergu-*

son v. Commissioner, 45 F. (2) 573, (C. C. A., 5), taxpayer in Texas negotiated oil leases as to 7/8ths of the mineral, retaining the remaining 1/8th interest, and received thereby a cash bonus and the royalties. Under the laws of Texas he made a sale in place of the 7/8ths interest, and his bonus-receipt was held subject to the Revenue Act provision imposing a special rate of tax upon the bonus as a capital gain from a sale, and his retained interest was held subject to depletion allowances as a property interest retained by him.

In *Alexander v. King,* 46 F. (2) 235, a taxpayer in Oklahoma claimed her royalty receipts described as "the equal 1/8th of all oil produced and saved" were subject to the capital gain provision. But in Oklahoma there can be no ownership of oil in place, and consequently no sale of same, and consequently the capital gain provision was inapplicable as there was no sale.

In *Berg v. Commissioner,* 33 F. (2) 641 (C. C. A. of D. of C.) and *Burkett v. Commissioner,* 31 F. (2) 667, responding to the contention that the capital gain provision should apply, it was held the instruments did not effect a sale and the provision could not be invoked.

Herein, where this Court finds a sale in place of the entire coal content, it follows, under the *Ferguson* case, that the profit, if any, is subject to be ascertained under the capital gain provision and not under the depletion provision of the Revenue Acts. But neither applies until the receipts have returned the capital value sold, and we have shown such return is not yet accomplished.

1(d) This Court has wrongly applied the law to the facts of the case.

This Court concludes, after discussion of various judicial precedents, that the several instruments effected sales of coal in place, and, nevertheless, the payments receivable as the proceeds of said sales, subject to depletion allowances, constitute taxable income, saying:

> "The Supreme Court has never abandoned the rule as to the effect of State decisions on questions of property; but it has held in some instances that State decisions do not cover the whole ground to which the Federal taxing statutes relate; and, in other instances that the statutes or decisions of the State lay down rules which define the property which Congress has undertaken to tax."

Respectfully, this conclusion is provoking in its indefinite statement. The Federal taxing statutes, as in the *Tyler* case, deal with a succession or transfer tax or death duty laid upon the happening of an event as distinguished from its tangible fruits; or they deal with a tax upon the tangible fruits, that is the taxable income, if any, realized from a transaction. In either case, the tax springs into existence upon the happening of an event. In case of income tax laws, as Mr. Justice Holmes says in *Weiss v. Wiener, supra:*

> "They do not charge for appreciation of property * * * unless realized in money by a sale."

Having a sale in the present case, as the only material factor, we do not believe this Court intends to say:

> "—it (the Supreme Court) has held in *cases of a sale* that state decisions do not cover the

> whole ground to which the *income tax* statutes relate; and in other *cases of a sale* that the statutes or decisions of the state lay down rules which define the property which Congress has undertaken to tax."

for if that is its meaning, we cannot apply the rule as any decision of the present case.

The coal-lands herein undoubtedly represented a capital asset, the sale of any part of which might be made, but the Revenue Acts nowhere define a sale. The Supreme Court has defined a sale as:

> "Ordinarily a transfer of property for a fixed price in money or its equivalent." *Five Per Cent Cases,* 110 U. S. 471.
>
> "Sale is a word of precise legal import both at law and equity. It means at all times, a contract between the parties, to give and to pass rights of property for money—which the buyer pays or promises to pay the seller for the thing bought and sold." *Williamson v. Berry,* 8 How. 495, 544.

As the word "sale" has an universal meaning, and as real property interests were sold in this case, in the absence of its definition in the Revenue Acts, resort must be had to the laws of West Virginia to determine the interest or title conveyed by the instruments, and this Court finds a sale in place was thereby made in 1901. It follows the vendor was thereby divested of ownership and interest, and that no interest is available for depletion allowances.

This Court refers to mining as a business and to royalties as income from same, and therefore subject to taxation. This is derived from *Strattons Independ-*

ence v. Howbert, 231 U. S. 399, rejecting the contention that:

> "—a mining corporation is not engaged in business, properly speaking, but is merely occupied in converting its capital assets from one form into another"—

but in that case the distinction applicable to this case is clearly stated:

> "The sale outright of a mining property might fairly be described as a mere conversion of the capital from land into money."

Having sold the coal content for money, herein the original vendor and its successor thereafter had no mine, no interest in a mining business, nothing but a claim for the purchase price as the result of conversion of its capital from land into money.

In *Stanton v. Baltic Mining Co.*, 240 U. S. 103, it is true the *Stratton* case was followed, but that does not make either decisive herein. In both those cases, the taxpayer was "*carrying on mining operations* * * * *upon mining lands owned by itself*", and engaged in a manufacturing process. In the *Stanton* case, it was contended the income tax fell upon the property and was prohibited by the Pollock rule; it was decided the XVI Amendment destroyed the Pollock precedent, and that as an excise tax same was not a direct tax upon property.

In *Von Baumbach v. Sargent Land Co.*, 242 U. S. 503, quoted by the Court, the situation is summarized in the opinion as follows:

> "We think that the payments made by the lessees to the corporations now before the Court

> were *not in substance the proceeds of an outright* sale of a mining property, but, in *view of the terms of these instruments, were in fact rents or royalties* to be paid upon entering into the premises and discovering, developing and removing the mineral resources thereof, and, as such, must be held now as then, to come fairly within the term 'income' as intended to be reached and taxed under the terms of the Corporation Tax Act." (Our italics.)

To complete our argument we cite *United States v. Biwabik M. Co.*, 247 U. S. 116, in which a lessee in Minnesota of iron ores is held, upon authority of the *Sargent* case to be *"in no legal sense a purchaser of ore in place"*, and not entitled to any depletion. By the *Sargent* case (the lessor) and the *Biwabik* case (the lessee), it appears neither lessor nor lessee was entitled to any depreciation under the Act of 1909, and, in *Lynch v. Alworth Stevens Co.*, 267 U. S. 364, this is plainly stated. The Revenue Act of 1916, however, provided a deduction for "exhaustion of property arising out of its use", and the *Lynch* case held same was not available alone to the lessor as the holder of title, but was available also to a lessee who had no title to the ore in place. This conclusion is placed on the ground that the right of the lessee to mine and remove the ore is property within the meaning of the statute.

In these authorities there is no direct definition of the depletion rights applicable to *proceeds of an outright sale,* but a distinction between such *proceeds* and mere *royalties* or rentals is evident. The Court carefully defines the receipts as not *proceeds of a sale,* or characterizes the taxpayer as *not a purchaser,* or as *with or without an interest* in the ore in place.

Hirschi v. United States, 67 Ct. Cl.; *Berg v. Commissioner,* 33 F. (2) 641, and *Burkett v. Commissioner,* 31 F. (2) 667, have some authority when the denial of certiorari is suggested. But the *Burkett* and *Berg* instruments do not appear to be more than leases and the decisions become immaterial. The *Hirschi* instrument is held not effective as a sale in place under the laws of Texas and the Court supports same by citation of *Steedman v. United States,* wherein certiorari was denied, but the *Steedman* case is expressly disapproved in *Crooks v. Harrelson,* 282 U. S. 55. The *Hirschi* case is in effect disapproved in *Group One Oil Corporation v. Bass,* 283 U. S. 279. The Court of Claims says in the Hirschi decision:

> "Congress in passing a revenue act does not, and is not called upon to suit the revenue system of the country to the varying and conflicting decisions and laws of the different states.

But in the later decision of *Poe, Collector, v. Seaborn,* 282 U. S. 101, the Supreme Court said:

> "These Sections (of the several Revenue Acts) lay a tax upon the net income of every individual. The Act goes no further, and furnishes no other standard or definition of what constitutes an individual's income. The use of the word 'of' denotes ownership. It would be a strained construction, which, in the absence of further definition by Congress, should impute a broader significance to the phrase." * * *
>
> "Said differences of state law, which bring a person within or without the category designated by Congress as taxable may not be read into the Revenue Act to spell out a lack of uniformity."

If the proceeds of a sale in place are not taxable when ascertained by the law of West Virginia, but, as proceeds of a lease, are taxable in another state, the return not subject to taxation in either case is the depletion allowance against same intended to return the capital outlay. There is no lack of uniformity for the vendee of the mineral in place takes the entire depletion deduction, while lessor and lessee divide same between them.

If the rule be that, notwithstanding a sale in place, the vendor is entitled to depletion, same conflicts with the established rule that depletion follows the property interest. It means the sole owner of the capital interest is partially deprived of the depletion deduction. It means a denial of final decisions to the contrary, and an allowance not authorized by law. It means confusion for the annual payments by the vendee are, as to him, capital investments not deductible from his gross income, *Jefferson Gas Coal Co. v. Commissioner*, 52 F. (2) 120 (C. C. A., 3), and as to the vendor they are rentals and not purchase-money receipts.

Rosenberger v. McCaughn, 25 F. (2) 699, is not rested upon the Supreme Court decisions in prior cases, but upon the ground that the calculation of income by the Commissioner as being within the payments received as proceeds of a sale in place is nowhere questioned and upon the ground—

> "—we think each payment represented in some measure both capital and increment, capital because it stood in the place of coal, and increment because in the payments running through ninety-nine years interest on the capital must inevitably have been included." • • •

This thought of the Court contravenes the settled rule stated with copious citation in *United States v. Merriam*, 263 U. S. 179:

> "On behalf of the government it is urged that taxation is a practical matter, and concerns itself with the substance of the thing upon which the tax is imposed, rather than with legal forms and expressions. But in statutes *levying taxes the literal meaning* of the words employed is most important, for such statutes are not to be *extended by implication* beyond the clear import of the language used. If the words are *doubtful*, the *doubt* must be *resolved against* the government and *in favor of the taxpayer* * * *."
>
> "I am not at all sure that in a case of this kind—a fiscal case—form is not amply sufficient; because as I understand the principle of all fiscal legislation, it is this: If the person sought to be taxed comes *within the letter of the law, he must be taxed*, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, *cannot bring the subject within the letter of the law, the subject is free, however, apparently within the spirit of the law the case might otherwise appear to be. In other words, if there be admissible in any statute what is called an equitable construction, certainly such a construction is not admissible in a taxing statute*, when you can simply adhere to the words of the statute."

It contradicts *Saunders v. Commissioner*, 29 F. (2) 832 (C. C. A., 3); *Platt v. Bowers*, 13 F. (2) 951; *United States v. Guinzberg*, 278 F. 363 (C. C. A., 2); *Park v. Gilligan*, 293 F. 129, and *Schneider v. Duffy*, 43 F. (2) 642, previously discussed in the brief of peti-

tioners. It contradicts *Logan v. Commissioner,* 42 F. (2) 193 (C. C. A., 2), as recently affirmed in *Burnet v. Logan,* 283 U. S. 404. These are decisions that subsequent payments upon rights to money established and accrued before the XVI Amendment are only the return and collection of capital without income increment.

From these several viewpoints, we submit the Court has not applied the precedents properly because same, under the different facts of this case, and under subsequent *stare decisis,* are inapplicable to the present case.

2(a) The depletion unit, being premised upon the expectancy of entire annual minimum payments, should apply to coal paid for instead of coal mined in the several years.

(b) The Courts have reversed the position of the Board as herein substantially adopted by this Court.

These points relate to the alternative position that depletion is allowable herein.

The Board ruling and the approved tax determination allow depletion only upon coal mined in any year instead of upon coal actually paid for. In presenting its tax determination so approved, respondent's counsel (R. 108) stated apologetically to the Board:

> "—in the respondent's computation allowances were computed at the rate of 3.6 cents per ton upon tonnage mined each year; that this method was in accordance with the opinion in this case, and consistent with the Board's rulings in other cases, *although the respondent in other cases was committed to the principle*

of allowing depletion on tonnage of coal paid for instead of upon tonnage actually mined in a taxable year." (Italics ours.)

The struggle of the Board against the position of respondent and taxpayers that depletion is allowable upon coal paid for and not merely upon coal mined, which would include depletion on any bonus or payment in excess of the price of coal mined, did not reach the courts for a long time, and when it did the Board was recently reversed in *Murphy Oil Co. v. Burnet*, — F. (2) — (January 11, 1932) (C. C. A. 9). Therein, respondent, by cross-petition, carried the issue to the Court, and obtained a most thorough and convincing opinion upon the question.

In the present case, the Board set out in its findings certain schedules of production and royalty payments, which this Court has approved. Petitioner (R. 109) submitted same demonstrated the minimum payments substantially exceeded the payment for coal mined, and offered to confirm the fact by the instruments themselves. The refusal of the Board to allow depletion upon coal paid for is a specific assignment of error.

The materiality of the question arises in three ways:

First. If petitioner receives $200 as a 10-cent per ton payment on 2,000 lbs. of coal, of which only 1,000 lbs. was mined, its depletion allowed is 1,000 × .036, or $36.00, instead of 2,000 × .036, or $72. In other words, its depletion allowance being limited to coal mined, same is not allowed against the payment of $100 made for coal not mined, and same is thereby considered by the Board opinion as a bonus not subject to depletion.

Second. In computing the depletion unit of 3.6 cents, the bonus excluded from its application is given effect, but such effect is disallowed in only allocating the depletion unit against coal mined. This requires some explanation. The respondent's basis for the 3.6 cent allowance is stated in this record (R. 93) as an estimate of 14,000,000 tons of recoverable coal with average mining tonnage of 350,000 tons indicating a mine-life of 40 years with an average annual income therefrom of $34,000. After 40 years, in other words, the entire receivables of petitioner from the instruments amount to $1,360,000, the present worth of which on March 1, 1913, is $510,000. This latter amount divided by 14,000,000 tons gives the unit of 3.6 cents per ton. This method is described in Articles 206 and 211 in petitioner's brief (p. 60). This brings us back to the first proposition as applied to the second. It is that 3.6 cents is based upon the minimum royalties as a factor of computation, but if $34,000 is received annually and only $17,000 of coal is mined, the effect is to allow a depletion only on $17,000, whereby $17,000 is deemed a bonus and is denied depletion. Another statement of the situation is that petitioner receives in effect 1.8 cents instead of 3.6 cents per ton upon the $34,000 payment.

Third. The statute with reference to depletion, being a special provision intended to return their capital to the owners of interests in mining properties, the money received for coal paid for involves such return and should be subject to the depletion allowance.

Turning to the schedules in the Board findings we find substantial excess payments under Leases 2 and 4 as follows:

Year	Mined	Paid for	Excess	Mined	Paid for	Excess	Mined	Paid for	Excess
1920...	57,189	120,000	62,811	86,918	100,000	13,082	19,231	187,500	168,269
1921...	54,660	120,000	65,340	15,297	100,000	84,703	25,024	306,250	271,226
1922...	55,864	120,000	64,136	.....	.....	.....	45,483	370,433	324,950
1923...	51,422	120,000	68,578	.....	.....	.....	74,152	340,782	266,630
1924...	57,928	120,000	62,072	.....	.....	.....	103,877	343,657	239,780
1925...	68,804	120,000	51,196	91,170	100,000	8,830	117,792	325,000	207,208
1926...	90,029	120,000	29,971	.....	.....	.....	153,717	335,115	181,408
			404,104			106,615			1,659,471

In these seven years petitioner is deprived of depletion upon 2,000,000 tons—that is, petitioner pays tax upon $72,000, and further analysis serves to increase the amount, although petitioner and respondent agree the decision is wrong and the only Circuit Court of Appeals that has considered the question says the decision is wrong. As we have quoted from *Nichols v. Coolidge, supra:*

"Taxes are very real things."

When respondent and his counsel go into Court in another case to sustain his Departmental position and succeeds, it seems unusual that they should stand precisely for a contrary position herein. The foregoing schedules found relevant by this Court demonstrate the substantial difference between coal paid for and coal mined. It becomes immaterial whether the coal paid for could subsequently be mined because the receipts therefor, considered as a bonus, are subject to depletion, and the rulings of the Board to the contrary have fallen away.

This Court does not in its opinion refer to this point, although petitioners argued same in their brief (pp. 66-70). It is submitted it goes to the very heart of this case and is entitled to consideration. Evidently the *Murphy Oil* decision in the Ninth Circuit is final for respondent has therein sustained his previous position, and has thereby obtained a reduction of the tax for the taxpayer, and both parties are satisfied. It is unfortunate that petitioner and respondent herein were not standing together in this Court against the Board, as they stood at its bar and urged that depletion, if any, was allowable by the statute in this case

upon coal paid for. It would be more unfortunate if either party failed to bring the situation to the attention of this Court.

(3) The Court erred in holding the West Virginia judgment is not res adjudicata as to the allowable amount of depletion.

In the Board findings it appears the West Virginia Collector was defended by the United States District Attorney and the General Counsel of respondent. It is a matter of judicial notice that the Collector and Commissioner are each officials of the Government in related capacities as the duties of both are concerned with the collection of the revenue. It is equally clear the Collector was defendant in the West Virginia action, and the Commissioner is the defendant herein, and that neither proceeding is directly against the United States.

In its original brief, petitioner did not argue the United States was the real defendant and respondent laid down the proposition that these appeals were really proceedings against the United States, citing *Sage v. United States.* The situation therefore arises that, admitting a judgment against a Collector is not *res adjudicata* against the United States, whether such judgment is or is not *res adjudicata* against the Commissioner.

This Court does not decide the Commissioner is in effect the United States, and, as apparently the Commissioner and Collector stand in the same relative positions, we do not believe it will so decide. If this is not really a proceeding against the United States,

and it is no more so than the proceeding against the Collector, then this Court falls into error in holding *Sage v. United States* is authority for holding the Commissioner is not bound by the judgment against the Collector.

Even though petitioners had maintained that the United States was really the opponent herein and in the West Virginia action, it follows that the *Sage* decision would deny the contention. Thereby the United States was not bound in the West Virginia judgment and was not the real party in interest. Whether the United States is the real party here remains an undecided question not reached by the *Sage* decision.

This Court, before falling into said error, said:

> "The rule (*res adjudicata*) is applicable, however, only when the subsequent suit is between the same parties or their privies."

and we proceed from this point.

That the Collector and Commissioner were privy in the West Virginia case is found by the Board. The record (p. 89) further recites a consent order signed by the District Attorney and Special Attorney for the Bureau of Internal Revenue as well as the attorneys for plaintiff, and a stipulation of facts and agreement that all papers should be received with the probative weight of testimony from witnesses. Thus the privity in fact is evident if sustained in law.

Here is the case of the respondent Commissioner cooperating with the defendant Collector in defense of the West Virginia action, although not a party of record in same.

In *Beyer Co. v. Fleischmann Co.*, 15 F. (2) 465, (C. C. A., 6), where a similar situation prevailed, we read:

> "The general rule is that one who prosecutes or defends a suit in the name of another, to establish or protect some interest of his own, or who openly assists in an action in aid of some such interest, to the knowledge of the opposing party, is as much bound by the judgment as he would be if he had been a party of record. Penfield *v.* Potts & Co. (6 C. C. A.), 126 F. 475, 61 C. C. A. 351; Greenwich Ins. Co. *v.* Friedman Co. (6 C. C. A.), 142 F. 944, 74 C. C. A. 114; Foote *v.* Parson, etc. (6 C. C. A.), 196 F. 951, 118 C. C. A. 105; Southern Pacific R. Co. *v.* United States, 168 U. S. 1, 18 S. Ct. 18, 42 L. Ed. 355; Souffront *v.* La Compagnie Des Suereries, 217 U. S. 475, 30 S. Ct. 608, 54 L. Ed. 846."

In *White v. Croker,* 13 F. (2) 321 (C. C. A., 5), the rule is again stated:

> "The rule under which one not named in a judgment may be bound thereby in consequence of participation in the suit in which the judgment is rendered is that one who prosecutes or defends a suit in the name of another to protect or establish his own right, or who assists in the prosecution or defense of an action in aid of some interest of his own, and who does this openly to the knowledge of the opposing party, is as much bound by the judgment, and as fully entitled to avail himself of it as an estoppel against an adverse party, as he would be if he had been a party to the record. Souffront *v.* Campagnie, etc., 217 U. S. 475, 30 S. Ct. 608, 54 L. Ed. 846."

In *Souffront v. Campagnie,* 217 U. S. 475, states the same rule:

> "The persons for whose benefit, to the knowledge of the court and of all the parties to the

> record, litigation is being conducted, cannot, in a legal sense, be said to be strangers to the cause. The case is within the principle that one who prosecutes or defends a suit in the name of another, to establish and protect his own right, or who assists in the prosecution or defense of an action in aid of some interest of his own, and who does this openly, to the knowledge of the opposing party, is as much bound by the judgment, and as fully entitled to avail himself of it, as an estoppel against an adverse party, as he would be if he had been a party to the record. Lovejoy *v.* Murray, 3 Wall. 1, 18 L. Ed. 129."

Further citation seems needless, as it is clear the Commissioner and Collector acted in concert in West Virginia and are equally bound by the result. Privity being admitted, it would reasonably follow the *res adjudicata* of the judgment as to the amount of depletion should be declared by the Court.

(4) The remanding of the Strother appeal is ineffective so far as compliance with the rulings in the Bankers appeal is required, unless said rulings be finally correct.

As the rights of Strother and other stockholders are dependent upon the decision in the case of their corporation, it follows such decision unless complete and correct in all material respects will only increase the error as affecting the stockholders.

If the corporation receipts as proceeds of sales in place effected before the XVI Amendment are not subject to tax, their distribution to stockholders is affected.

If, in the alternative, such receipts are subject to depletion allowances, such allowances must be correct to be properly effective.

If receipts measured by coal paid for but not mined are a bonus, whether same is or is not subject to depletion is material.

These relations between the case of the corporation and the stockholder emphasize the importance of finding the correct answer to the questions raised in these cases.

They demonstrate the propriety of the stockholder joining in this application for rehearing.

In Conclusion.

We respectfully submit as material error the failure of the Court to find:

1. That, as a sale in place is admitted to have taken place before passage of the XVI Amendment, the receipt of proceeds of the certain accrued claim, as paid thereafter, is a return of capital without income; capital is to be fully returned before income subject to tax can be ascertained.

2 (*a*) Alternatively, depletion is a special statutory allowance awarded to the owner of an interest in property. Where the interest is terminated by a sale in place, there can be no remaining interest sufficient to measure a depletion allowance in the proceeds of the sale.

2 (*b*) Alternatively, depletion allowances, if any, exist against all receipts from the depletable interest, including any bonus payment, and in these cases will

apply to coal paid for and not merely to coal mined in the several years.

3. Alternatively, depletion allowances, if any, herein as *res adjudicata* through the privity of the Collector and Commissioner in defending the West Virginia action.

We submit the Strother appeal must abide the reconsideration of the opinion in the Bankers case.

We submit any other error, of incidental nature, will disclose itself upon further consideration of the foregoing matters by the Court.

Respectfully submitted,

WELLS GOODYKOONTZ,
AMDEN R. McATEE,
Attorneys for Petitioners,
Bankers Pocahontas Coal Co.,
D. J. F. Strother.

Certificate of Counsel.

We, Camden R. McAtee and Wells Goodykoontz, attorneys of record for the petitioners in the above styled cases for review, do hereby certify that the foregoing petition for rehearing is presented in good faith and not for the purposes of delay.

(S.) CAMDEN R. McATEE,
(S.) WELLS GOODYKOONTZ,
Attorneys for Petitioners,
Bankers Pocahontas Coal Co.;
D. J. F. Strother.

ORDER DENYING REHEARING.

Filed and Entered March 7, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS,

FOURTH CIRCUIT.

No. 3215.

Bankers Pocahontas Coal Company, Petitioner.

vs.

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

This Court having at its January term, 1932, rendered its decision affirming the decision of the said Board of Tax Appeals in this cause except as to the determination of the deficiencies of the corporation for the year 1924, and as to this year remanding said cause to the United States Board of Tax Appeals for further proceedings in accordance with the opinion of the Court filed herein, and the petitioner having on February 26, 1932, presented to the Court a petition for a rehearing of the said cause, and the same having been carefully considered,

It Is Now Here Ordered by this Court that the rehearing asked for, be, and the same is hereby, denied.

Let mandate issue after the expiration of five days from this date.

March 7, 1932.

JOHN J. PARKER,
Senior Circuit Judge.

March 11, 1932, petition of petitioner for a stay of the mandate is filed.

Same day, order staying the mandate is filed.

MOTION FOR LEAVE TO FILE SUPPLEMENTAL PETITION FOR REHEARING AND REARGUMENT.

Filed in Open Court April 12, 1932.

(Style of Court and Title Omitted.)

Come now petitioners in the above entitled proceeding, by their attorneys, and tender their supplemental petition for rehearing and reargument, and move the Court for leave to file same, and to fix a date for hearing the parties on same.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

SUPPLEMENTAL PETITION OF PETITIONER FOR REHEARING.

Filed by leave granted in Open Court April 12, 1932.

United States Circuit Court of Appeals for the Fourth Circuit

No. 3214

D. J. F. STROTHER, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

No. 3215

BANKERS POCAHONTAS COAL COMPANY, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT.

(Consolidated for Hearing.)
(Before Parker and Soper, Circuit Judges, and Baker, District Judge.)

ON PETITIONS TO REVIEW DECISIONS OF UNITED STATES BOARD OF TAX APPEALS.
Argued October 20, 1931.
Decided January 25, 1932.
Petition for Rehearing Overruled.

SUPPLEMENTAL PETITION FOR REHEARING AND FOR ORAL ARGUMENT IN SUPPORT OF PETITION FOR REHEARING BY BOTH PETITIONERS.

Under Court Rule No. 29.

FILED APRIL 12, 1932.

By leave of Court therefor asked and granted: Petitioners respectfully request—

(1) A reconsideration of the denial of the Petition for Rehearing heretofore filed on February 26, 1932.

(2) Opportunity by oral argument to present reasons for said rehearing.

For cause:

(*a*) Court Rule 29, providing a petition for rehearing "will not be granted, or permitted to be argued, unless a judge who concurred in the judgment desires it and a majority of the Court so determined," was construed by counsel to intend that the Court, as constituted at the hearing would *en banc* consider such petition. Accordingly, it was the impression the Court would not so sit together until April, 1932, at Richmond, Virginia. Consequently, no request for oral hearing upon the petition, and no brief in elaboration of reasons therefor was believed to be required until the Court would sit in April, 1932.

(*b*) Only after decision of these cases on January 25, 1932, did the petitioners and attorneys receive the opinion for their consideration.

On February 8, 1932, stay of the mandate was ordered on condition that within 30 days petition for rehearing be filed or application be made for certiorari to the Supreme Court. Petitions for rehearing were duly filed by both parties, and were denied on March 7, 1932, with direction for issue of mandate after five days.

On March 11, 1932, this Court ordered a stay of mandate for 60 days pending application for certiorari.

(* * * "unless otherwise ordered by this or the Supreme Court, and provided said application is filed in said Supreme Court within 60 days from this date.")

Thus, between the date of decision on January 25th and denial of rehearing on March 7, 1932, within 42 days, the petition for rehearing and its denial occurred, at a time of year and under present business conditions when the Court and counsel and litigants were necessarily engaged in giving attention and time to other important affairs of public and private character.

(*c*) As the right to change the order for stay of the mandate (quoted above) is reserved, the propriety of a rehearing is still believed to rest in and with the Court and may properly be granted if good and sufficient ground is shown therefor.

(*d*) This Court was created and constituted as a relief tribunal to the Supreme Court and strives to relieve that other great Court of the heavy labor imposed upon it, unless and until it feels bound as to finality of disposition of causes before it, when subsequent holdings after presentation of cases may and do occasion as here further consideration of fact or law.

(*e*) This decision and opinion are based on rules of law herein not pertinent to the facts, particularly in holding rules of taxation as to income of mines and their products determine the case when only real estate and its sale, *and not mines and their products,* is the subject matter presented herein. Verbal explanation is essential to presentation of a due understanding of the facts and to show the methods of income determi-

nation approved herein as applicable to the facts of these cases find no justification in the Revenue Acts.

(*f*) That the points made against the decision and opinion in the petitioners' Petition for Rehearing and their briefs, especially their Reply Brief, upon oral presentation of their soundness, will demonstrate the propriety of a holding contrary to the pronounced decision.

(*g*) That the decision of these cases according to law upon the rights involved presents or creates no precedent in taxation, as their facts indicate their concern with a deplorable coal land condition pointing to future decreases of the purchase money payments derived from sales made before the effective date of the XVI Amendment.

(*h*) That the orders of the Court as to further disposition of the cases entail further delay to that now accrued in disposing of them. Congress may not impose excessive fines (Article VIII, Constitution), yet herein large levies against capital assets, which are not income or profits accrued after 1913, have been required and satisfied, and carry additional penalties while the power so to tax said assets is in litigation these past twelve years.

This attrition through tax and penalty and incidental expense, merely because taxpayers are legally and by due process contesting the rights asserted against them, demonstrates the power to tax is the power to destroy, and that industry will languish under the oppression of taxes levied in the name of progress.

(*i*) The denial of certiorari by the Supreme Court in any case, wherein the findings appear to modify or contradict previous decisions of the Supreme Court does not establish nor approve such modification or contradiction. In *Atlantic C. L. Co. v. Powe,* 283 U. S. 401, 75 L. Ed. 1142, answering this precise question the Court quoted from its opinion in *United States v. Carver,* 260 U. S. 482, 67 L. Ed. 361, wherein it decided:

> "The denial of a writ of certiorari imports no expression of opinion upon the merits of the case, as the bar has been told many times. Therefore it is unnecessary to consider whether the libellants' argument is supported by the decisions to which they refer."

(*j*) The *briefs* filed by the litigant parties did not refer to, nor did the *opinion* of this Court cite certain Federal Court decisions *reported* since the date of the decision. Evidently neither the Court nor counsel had those decisions before them at or before the decision or the order denying rehearing; said decisions are:

Commissioner v. Brown, 54 F. (2) 563 (Federal Reporter Feb. 22, 1932).

Old Colony Railroad Co. v. Commissioner, U. S. Supreme Court Advance Ops. No. 7, 1931 Term, p. 317; 76 L. Ed. 317.

Crile v. Commissioner, 55 Fed. (2) 804 (Federal Reporter April 4, 1932).

Hernandez, Collector, v. Becker, 54 F. (2) 542. (Federal Reporter Feb. 22, 1932).

Harmel v. Commissioner, — Fed. (2) —, (Federal Reporter, — 1932).

Second National Bank v. Woodworth, 54 F. (2) 672 (Federal Reporter February 22, 1932).
Murphy Oil Co., v. Commissioner, 55 F. (2) 17 (Federal Reporter, March 21, 1932).

Brief reference is here made to these recent decisions:

Petitioners contend that before the incidence of the XVI Amendment they owned the right to receive the purchase money contracted to be paid by the purchasers of coal sold to said purchasers in 1902, upon the basis of the coal thereafter taken out of the stratum or coal seam, and the liability of petitioners to income tax upon such contract receipts is the controversial subject. The claim to said receipts, *if an unconditional obligation* existing on and before passage of the XVI Amendment, when subsequently collected, does not constitute taxable income, this being the general rule. In *Commissioner v. Brown,* 54 F. (2) 563 (C. C. A.-1), such a claim, *existing as a conditional obligation,* is held not to be income when subsequently collected, upon authority of *Burnet v. Logan,* 283 U. S. 404. These decisions read together, or separately, are an all sufficient solution of the present cases.

Petitioners contend that, having prior to the XVI Amendment and Revenue Acts made contracts and thereby sold realty and passed the title to same, the subsequent payments do not constitute taxable income, and *Old Colony Railroad Co., v. Commissioner,* U. S. Supreme Court Adv. Op. 7, 1931 Term, 317, supports this position. The second, third, fourth and fifth headnotes of that decision are:

Second. "Premiums received on corporate bonds issued *prior* to the effective date of the Sixteenth Amendment to the Federal Constitution, authorizing Federal taxation of incomes, *may not* be made the *basis* of subsequent income taxation, although the Interstate Commerce Commission has required them to be amortized over the period of the respective lives of the bonds and a yearly ratable proportion thereof to be reported as income."

Third. "The amount of interest on bonded indebtedness which may be deducted from gross income in determining taxable income is the amount *contracted to be paid,* notwithstanding the fact that as the bonds were issued at a premium, the effective rate is less."

Fourth. "The legislature must be presumed to use words in their known and ordinary significance; and this rule is applicable to taxing acts."

Fifth. "Terms used in tax statutes are, in case of *doubt,* to be given the construction *most favorable* to the taxpayer."

Mr. Justice Roberts' reasoning in the opinion squares with the holdings referred to in the above cited cases and means that when payments are received or *contracted* to be received before taxing acts come into being, those payments can not be made a proper *basis* of *taxation* by subsequent legislation.

Petitioners contend the contract payments collected in the taxable years are not subject to tax as the realization of obligations created and existing before the XVI Amendment. In *Crile v. Commissioner,* 55 Fed.

(2) 804, (C. C. A.-6), a sum of money was paid to taxpayer as part consideration of a lease and the Court says:

> "Where, there is an intent to create in the 'lessee' an interest in the property itself—as by way of purchase,—even though that interest may be forfeitable by failure to perform conditions subsequent, and this intent is made manifest by the instruments duly executed to carry it into effect, the attending payment is a return of capital, and should be so regarded, at least prior to forfeiture and reversion."

Therefore, as there was here an admitted sale, the payment of purchase money is a return of capital. As the vendor is without further interest in the property neither he nor his assigns can claim depreciation or depletion as to the property conveyed.

Petitioners raised the point that for all purposes, including purposes of taxation, the statutes and rules of property in a state were controlling in the Federal Courts. This Court's decision and opinion discounts this contention, yet in *Hernandez, Collector v. Becker,* 54 F. (2d) 544, dealing with a federal estate tax, Judge Phillips held the character of the estate from which the federal tax came was controlled by the statutes and rules of property of the state.

In *Harmel v. Commissioner,* Fed. (2) (C. C. A.-5), the rule that an oil and gas lease conveys a determinable fee to minerals in place under the Texas laws and rules of property is expressly upheld, and the special capital gain provision instead of the general tax upon ordinary income, as provided in the Revenue Acts, is

held to measure the income tax liability upon the resulting gain to the taxpayer.

Petitioners raised the point that the Collector and the Commissioners were in privity and a judgment against one was binding against the other. This Court discredited that position, yet *Second National Bank v. Woodworth,* 54 F. (2) 672 (Judge Simons) holds a collector of internal revenue is agent or trustee for the government and refers to and discusses at length Mr. Justice Holmes' decision in the *Sage* case, relied on in the opinion (250 U. S. 33), and his remarks are applicable to the instant cases:

> "There is an important distinction between the facts of the case at bar and those of the *Sage* case."

The distinction in the *Woodworth* case is that the judgment put forward in bar by the Collector is one against the United States, whereas in the *Sage* case the judgment so put forward by the United States was against the Collector. In the *Woodworth* case, the judgment in bar is held sufficient on the ground that, as the suit is against the Collector by reason of his official acts as a public officer and official agent or trustee of the Government, therefore:

> "It may be conceded that a judgment against an agent does not bind the principal, but that is not to say that the converse is true, and that a judgment against the principal is not a bar against the agent, where the latter is privy with the former in respect to the subject matter of the suit."

Judge Simon, after suggesting the argument of Mr. Justice Holmes is *dicta,* rests his decision not directly upon *Sage v. United States,* but upon *Bank of Kentucky v. Stone,* 174 U. S. 799, 43 L. Ed. 1187, wherein a judgment enjoining a town from enforcing a tax was held to bar a similar proceeding against its board of assessors.

In these present cases, the judgment is against the Collector, the agent and not the principal, the United States. That a judgment against its officer is not conclusive upon the United States has long been settled on the basic grounds that the Government cannot be sued without its consent that its officers may not waive this immunity, and that the Government cannot be compelled into Court to litigate with private parties in defense of its property, as decided in *Carr v. United States,* 98 U. S. 433, 25 L. Ed. 209. But that its officer may be sued and that its other officer in privity in the matter and aiding in defending the proceeding may be, and is, bound by the ensuing judgment, is not to say that the Government is likewise bound. But saying the Government is not bound is no justification for concluding its other officer is not bound. Thus, in *Johnson v. Herold,* 161 Fed. 593, 602, sixteen actions for recovery of identical taxes were brought against various collectors by the plaintiff, and a judgment in one case was held conclusive in the others, thus binding plaintiff or the collector not a party to the decided cause.

Without further quotation from the *Woodworth* opinion, attention is invited to the analysis of the *Sage* case in this most recent, well considered opinion, particularly the last paragraph and it would seem clear

that by reason and decision of the very highest court there is privity which should be recognized between *White, Collector,* and the *Commissioner of Internal Revenue* over the same subject matter—both are agents and trustees for the United States. In one case the tax illegally collected is returned, and in these cases the Commissioner is endeavoring to collect another illegally imposed tax. Both acts are by the agents and trustees of the principal. The agents are not personally liable. The right and reason of the *Woodworth* case is apparent.

Petitioners contend, if depletion is computable as an allowable deduction herein, same should be upon the basis of coal paid for and not of coal mined, pointing out that respondent took the same position before the Board. The Petition for Rehearing (pp. 22-26) discusses this issue, with some reference to *Murphy Oil Co. v. Burnet,* 55 F. (2) 17 (C. C. A.-9), wherein on January 11, 1932, the Board's position was held erroneous that payments for coal not mined constituted bonuses not subject to depletion allowances. This ruling was obtained by petition for review filed by respondent.

Judge Wilbur justifies this ruling first on the facts of the *Murphy* case, and then upon the development of the depletion principle as developed in statute, decision and regulation, and utterly destroys the Board concept which this Court has approved in its affirmance of the Board. He concludes:

> "The statute, with reference to depletion * * * is a special one * * * involving the pro-

> duction of oil and minerals from mines, and the consequent *return of capital by the owners of interests therein,* and controls over other general provisions of the law in regard to the return of capital investment." (Our italics.)

But, as decided above, a sale of mineral in place in Texas creates a determinable fee in the purchaser and the profit is taxable as a capital gain. As this Court has likewise decided, a sale of mineral in place in West Virginia was effected herein in 1902. As said in the *Crile* decision, *supra,* the creation of an interest in the "lessee" made the consideration a return of capital. It follows petitioners are not the owners of any interests in the mines or coal, and cannot avail themselves of depletion allowances, nor have same forced upon them.

In Conclusion.

This application is lengthy and yet incomplete, and full understanding of the facts and law depend upon verbal presentation and discussion of their aspects that the simple truth may appear. But the present and future stress of the taxpayers make such application imperative, and, with due apology that no imposition upon the time or patience of the Court or its members is intended, still these requests are made:

1. That this petition and application be permitted to be filed.

2. That opportunity be granted the parties to appear at an early date and orally present argument as to the propriety of a rehearing.

3. That upon rehearing the petitioners be declared not liable for income and profits taxes upon the contract proceeds from the sales of coal in place effected before the XVI Amendment.

Respectfully submitted,

D. J. F. STROTHER,
BANKERS POCAHONTAS
COAL CO.,
Petitioners.

By WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys.

Certificate of Counsel.

We, Wells Goodykoontz and Camden R. McAtee, attorneys of record for the petitioners in the above styled cases for review, do hereby certify that the foregoing petition for rehearing is presented in good faith and not for the purposes of delay.

(S.) WELLS GOODYKOONTZ,
(S.) CAMDEN R. McATEE,
Attorneys for Petitioners,
Bankers Pocahontas Coal Co.,
D. J. F. Strother.

ORDER DENYING REHEARING AND STAYING MANDATE.

Filed and Entered April 29, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS,

FOURTH CIRCUIT.

No. 3215.

Bankers Pocahontas Coal Company, Petitioner.

vs.

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

On Consideration of the supplemental petition of the petitioner for a rehearing of the above entitled cause, filed by leave of Court on April 12, 1932,

It Is Now Here Ordered by this Court that the rehearing asked for in the supplemental petition be, and the same is hereby, denied.

It Is Further Ordered that the mandate of this Court in this cause be, and the same is hereby, stayed pending the application of the petitioner in the Supreme Court of the United States for a writ of *certiorari* to this Court, unless otherwise ordered by this or the said Supreme Court, and provided said application is presented in the said Supreme Court on or before May 23, 1932.

April 29, 1932.

JOHN J. PARKER,
Senior Circuit Judge.

CLERK'S CERTIFICATE.

UNITED STATES OF AMERICA,
Fourth Circuit, ss:

I, Claude M. Dean, Clerk of the United States Circuit Court of Appeals for the Fourth Circuit, do certify that the foregoing is a true copy of the record and proceedings in the therein entitled cause, as the same remain among the records and files of the said Circuit Court of Appeals.

IN TESTIMONY WHEREOF, I hereto set my hand and affix the seal of the said United States Circuit Court of Appeals for the Fourth Circuit, at Richmond, Virginia, this 7th day of May, A. D., 1932.

(Seal of Court)

CLAUDE M. DEAN,
Clerk U. S. Circuit Court of Appeals, Fourth Circuit.

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 10, 1932

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit is granted, and the case is assigned for argument immediately following case No. 80, Murphy Oil Co. vs. Burnet, Commissioner of Internal Revenue.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

Endorsed on cover: File No. 36,801. U. S. Circuit Court of Appeals, Fourth Circuit. Term No. 104. Bankers Pocahontas Coal Company, petitioner, vs. Commissioner of Internal Revenue. Petition for writ of certiorari and exhibits thereto. Filed May 23, 1932. File No. 36,801.

CLERK'S COPY.

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1932

No. 105

D. J. F. STROTHER, PETITIONER,

vs.

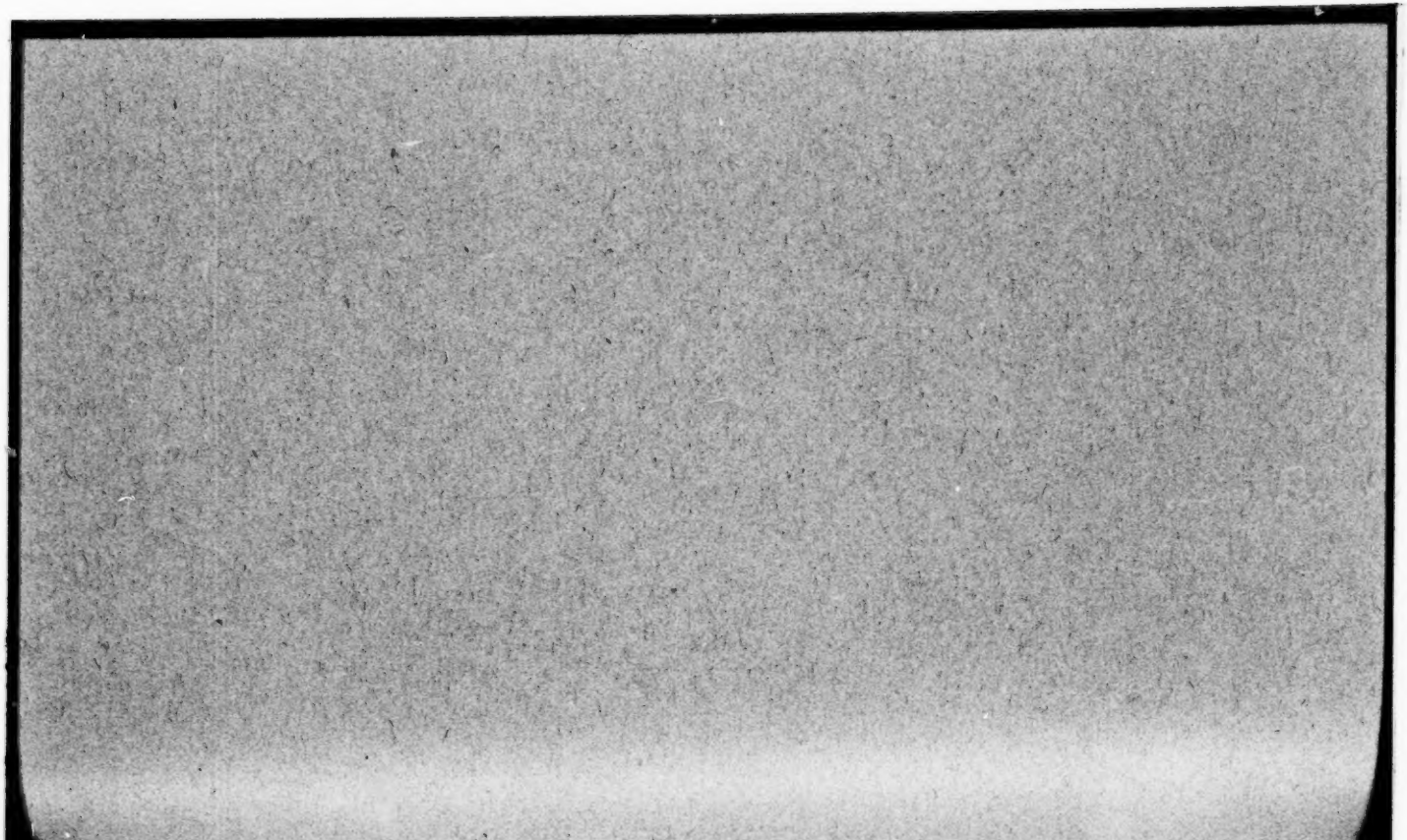
COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

PETITION FOR CERTIORARI FILED MAY 23, 1932

CERTIORARI GRANTED OCTOBER 10, 1932

(36,802)



(36,802)

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1932

No. 105

D. J. F. STROTHER, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

INDEX

	Page
Proceedings before U. S. Board of Tax Appeals	1
Docket entries #10472	1
Docket entries #25275	4
Docket entries #32170	6
Petition #10472	7
Deficiency letter #10472	10
Answer #10472	13
Statement re petition, etc., #25275	14
Deficiency letter #25275	15
Statement re petition, etc., #32170	21
Deficiency letter #32170	21
Findings of fact and opinion, Smith, M	25
Motion for rehearing and modification	46
Order denying motion for rehearing	48
Respondent's notice of settlement	49
Order withholding settlement	56
Petitioner's objections and counter-proposal	57
Petitioner's amended counter-proposal	64
Petitioner's supplemental counter-proposal	69

JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., OCTOBER 26, 1932

Page

Order amending findings 70
Decision 71
Petition for review 72
Statement of evidence 79
Testimony of D. J. F. Strother 80
Præcipe for transcript of record 87
Agreed order re single record 90
Certificate of clerk 92
Proceedings in United States circuit court of appeals, fourth circuit .. 93
Docket entries 93
Opinion, Soper, J. 95
Judgment 111
Petition for rehearing by petitioner 112
Petition for rehearing by respondent 139
Order denying rehearings 141
Motion for leave to file supplemental petition for rehearing 142
Petitioner's supplemental petition for rehearing 143
Order denying rehearing and staying mandate 154
Clerk's certificate 155
Order allowing certiorari 157

TRANSCRIPT OF RECORD

Docket No. 10472

APPEARANCES:

For Petitioner:
Camden R. McAtee, Esq.,

For Respondent:
W. F. Gibbs, Esq.,
M. E. McDowell, Esq.,
F. B. Schlosser, Esq.

D. J. F. Strother, Petitioner,

vs.

Commissioner of Internal Revenue,
Respondent.

DOCKET ENTRIES

1925
Dec. 30—Petition received and filed.

1926
Jan. 6—Copy of petition served on Solicitor.
Jan. 6—Notification of receipt mailed taxpayer.
Jan. 21—Answer filed by Solicitor.
Jan. 27—Copy of answer served on taxpayer—assigned to General Calendar.
Apr. 29—Motion to consolidate for hearing with 25275 filed by General Counsel.

1927
May 10—Hearing set on motion June 27, 1927. (See 25275).
June 27—Hearing had before Mr. Green on respondent's motion to consolidate with 25275. Granted.

June 28—Order motion to consolidate be granted; proceeding remain on General Calendar signed and filed. Both sides notified.
Sept. 8—Motion to consolidate for hearing with dockets 18679, 18680, 26655, 26656, 25275, 14516 and 14517, filed by taxpayer. See 18679. Granted 9/8/27.

1928
June 27—Hearing set 9/11/28.
July 19—Motion for a continuance to Oct. 10, 1928, filed by taxpayer. See 18679. Granted 7/23/28.
Oct. 9—Motion for a continuance of 60 days filed by taxpayer. See 14516. Granted to 12/10/28.
Dec. 6—Motion for a continuance to Feb. 15, 1928, filed by taxpayer. See 18679.
Dec. 8—Motion for a continuance granted to 2/19/29.

1929
Jan. 28—Motion for a continuance to 4/15/29 filed by taxpayer—granted.
Mar. 22—Motion for a continuance to 5/2/29 filed by taxpayer. 3/25/29 granted.
May 2 & 3—Hearing had before Mr. Smith. Heard with 25275, 32170, 14516, 14517 and 42664. Briefs due 90 days from date.
May 20—Transcript of hearing May 2 and 3, 1929 filed.
July 17—Motion for extension of 30 days from Aug. 1, 1929 to file briefs (both parties) filed by
(2) General Counsel.
July 19—Motion for extension of 30 days granted.
Aug. 28—Brief filed by General Counsel.
Aug. 31—Motion for extension to Sept. 10, 1929 to file brief filed by taxpayer.
Sept. 4—Motion granted.
Sept. 10—Requested findings of fact and brief filed by taxpayer.

1930
Jan. 22—Findings of fact and opinion rendered by Chas. P. Smith, Division 5. Judgment will be entered under Rule 50.
Feb. 27—Motion for rehearing and modified findings of fact and opinion filed by taxpayer.

Mar. 6—Order denying motion of Feb. 27 for rehearing entered.
Mar. 31—Notice of settlement filed by General Counsel.
Apr. 4—Hearing set Apr. 23, 1930, on settlement.
Apr. 21—Motion for continuance of 30 days on settlement filed by taxpayer. 4/22/30 granted and set for hearing May 21, 1930.
May 21—Motion for order to withhold determination pending 14516, filed by taxpayer.
May 21—Order for continuance to June 18, 1930 on Rule 50 entered.
May 24—Transcript of hearing of May 21, 1930, filed.
June 18—Hearing had before Mr. Smith on proposed redetermination under Rule 50.
July 1—Transcript of hearing of 6/18/30 filed.
July 15—Order that hearing under Rule 50 be continued to Day Calendar of Aug. 13, 1930 entered.
July 15—Order that motion for rehearing be denied entered.
Aug. 12—Objections and counter-proposal under Rule 50 filed by taxpayer.
Aug. 13—Hearing held before Mr. Trammell on settlement under Rule 50. Continued Sept. 3, 1930.
Aug. 13—Order entered continuing to Sept. 3, 1930.
Sept. 2—Amended counter proposal Rule 50 filed by taxpayer.
Sept. 3—Hearing held before Mr. Smith, Division 5, on settlement under Rule 50. Contested and argued. Taken under advisement.
Sept. 10—Supplement to amended counter proposal Rule 50 filed by taxpayer.
Sept. 23—Transcript of hearing of Sept. 3, 1930 filed.
Sept. 26—Order that last paragraph of findings of fact be deleted and revised, paragraph be substituted, entered.
Sept. 29—Decision entered, Chas. P. Smith, Division 5.

1931
Jan. 6—Petition for review to U. S. Circuit Court of Appeals, 4th Circuit, with assignments of error filed by taxpayer.
Feb. 28—Certified copy of order granting 60 day extension to prepare and deliver record filed.

Apr. 24—Certified copy of order granting 60 days extension to prepare and deliver record filed.
June 27—Certified copy of order granting 30 day extension to prepare and deliver record filed.
July 11—Copy of order from U. S. Circuit Court of Appeals (4th) to transmit single record to
(3) Court filed.
July 14—Agreed praecipe filed.
July 14—Agreed statement of evidence approved and ordered filed.

(4) Docket No. 25275.

APPEARANCES:

For Petitioner:
Camden R. McAtee, Esq.,

For Respondent:
W. F. Gibbs, Esq.,
M. E. McDowell, Esq.,
F. Schlosser, Esq.

D. J. F. Strother, Petitioner,

vs.

Commissioner of Internal Revenue,
Respondent.

DOCKET ENTRIES

1927
Mar. 16—Petition received and filed. Taxpayer notified.
Mar. 17—Copy of petition served on General Counsel.
Apr. 29—Motion to join with 10472 for hearing filed by General Counsel.
Apr. 29—Answer filed by General Counsel.
May 2—Copy of answer served on taxpayer—General Calendar.
May 10—Copy of motion served on taxpayer—assigned to 6/27/27.
June 27—Hearing had before Mr. Green on respondents motion to consolidate with 10472—granted.

June 28—Ordered motion be granted, signed and filed. Both sides notified.
Sept. 8—Motion to consolidate for hearing with dockets 18679, 18680, 26655, 26656, 10472, 14516 and 14517 filed by taxpayer. See 18679. Granted.

1928
June 27—Hearing set 9/11/28.
July 19—Motion for a continuance to Oct. 10, 1928 filed by taxpayer. See 18679. Granted 7/23/28.
Oct. 9—Motion for a continuance of 60 days filed by taxpayer. See 14516.
Oct. 11—Motion granted to 12/10/28.
Dec. 6—Motion for a continuance to Feb. 15, 1929 filed by taxpayer. See 18679.
Dec. 8—Motion for a continuance granted to 2/19/29.

1929
Jan. 28—Motion for continuance to 4/15/29 filed by taxpayer—granted.
Mar. 22—Motion for continuance to 5/2/29 filed by taxpayer. See 18679.
May 2 & 3—Hearing had on merits before Wm. R. Green, Division 13. Heard with 14516-17, 10472, 42664 & 32170. Briefs due 90 days from date.
May 20—Transcript of hearing May 2 & 3, 1929 filed.
July 17—Motion for extension of 30 days from Aug. 1, 1929 to file briefs (both parties) filed by General Counsel.
July 19—Motion for extension granted.
Aug. 28—Brief filed by General Counsel. See 10472.
Aug. 31—Motion for extension of 10 days to file brief filed by taxpayer. See 10472.
Sept. 4—Motion granted.
Sept. 10—Requested findings of fact and brief filed by taxpayer.

1930
Jan. 22—Findings of fact and opinion Chas. P. Smith, (5) Div. 5. Judgment will be entered under Rule 50.

Subsequent Docket Entries are identical with those in Docket 10472 as appearing herein, and are here omitted.

(6) Docket No. 32170.

APPEARANCES:

For Petitioner:
Camden R. McAtee, Esq.,

For Respondent:
W. F. Gibbs, Esq.,
F. Schlosser, Esq.,
M. E. McDowell, Esq

D. J. F. Strother, Petitioner,

vs.

Commissioner of Internal Revenue,
Respondent.

DOCKET ENTRIES

1927
Nov. 5—Petition received and filed. Taxpayer notified (fee paid).
Nov. 5—Copy of petition served on General Counsel.
Nov. 5—Motion to consolidate for hearing with docket 18679 filed by taxpayer. See 18679.
Dec. 22—Answer filed by General Counsel.

1928
Jan. 3—Copy of answer served on taxpayer—assigned to General Calendar.
Oct. 9—Motion for a continuance of 60 days from 10/10/25 filed by taxpayer. See 18679.
Oct. 11—Motion granted to 12/10/28.
Dec. 6—Motion for a continuance to Feb. 15, 1929 filed by taxpayer. See 18679.
Dec. 8—Motion for a continuance granted to 2/19/29.

1929
Mar. 29—Motion for a continuance to May 2, 1929, filed by taxpayer. 3/30/29 granted.

May 2 & 3—Hearing had before Mr. Smith. Heard with 14516-17, 10472, 25275, 42664. Briefs due 90 days from date.
May 20—Transcript of hearing May 2 and 3, 1929 filed.
July 17—Motion for extension of 30 days from Aug. 1, 1929 to file brief (both parties) filed by General Counsel.
July 19—Motion for extension granted.
Aug. 28—Brief filed by General Counsel. See 10472.
Aug. 31—Motion for 10 days extension to file brief filed by taxpayer. See 10472.
Sept. 4—Motion granted.
Sept. 10—Requested findings of fact and brief filed by taxpayer.

1930
Jan. 22—Findings of fact and opinion rendered by Chas. P. Smith, Division 5, judgment will be entered under Rule 50.

Subsequent docket entries are identical with those in Docket 10472 as appearing herein, and are here omitted.

PETITION

(7) Filed Dec. 30, 1925.

UNITED STATES BOARD OF TAX APPEALS

In re: Appeal of
D. J. F. Strother,
Welch, West Virginia.

Docket No. 10472

The above-named taxpayer hereby appeals from the determination of the Commissioner of Internal Revenue set forth in his deficiency letter of November 9, 1925, (IT:PA-1-KB-107-60D), and as the basis of his appeal sets forth the following:

1. The taxpayer is an individual, residing at Welch, West Virginia.

2. The deficiency letter was mailed to taxpayer on November 9, 1925, and a copy of same is attached.

3. The taxes in controversy are income taxes for the calendar years 1919, 1920 and 1921, being an aggregate of $3,268.12 and are less than $10,000.

4. A determination of the tax contained in the said deficiency letter is based upon the following errors:

(a) Additions to the income of taxpayer in the several years as follows:

1919	$10,394.50
1920	11,891.30
1921	13,370.26

5. The facts upon which the taxpayer relies as the
(8) basis of his appeal are as follows:

Taxpayers reports upon a cash receipts and disbursements basis. Taxpayer for the several years, was and is an officer and stockholder of the Bankers Pocahontas Coal Company, a corporation at Welch, West Virginia. Taxpayer received from said corporation, distributions in the several years respectively in the amounts above set out. Taxpayer alleges and charges same and each of them are distributions of capital and are not income, and hence are not taxable to taxpayer as income. Before March 1, 1913, said corporation had acquired the fee simple to coal lands in West Virginia, with reference to which, leases were theretofore made and outstanding whereby the lessee obtained and held the right to mine all coal covered by its special lease until exhaustion as a fixed tonnage price per ton, being required to pay a minimum amount each year and entitled thereafter to mine any coal so paid for without additional charge. By said leases the predecessors of said corporation had divested themselves of the coal as said leases are legally in West Virginia sale of coal in place, and the land divested of said coal was and is without value. Said corporation therefore on March 1, 1913 held said leases or choses in action as its sole property of value and any return there-
(9) after, in periodical payments was and is a return of capital and not of income. Consequently, taxpayer receiving such returns by distribution from the taxpayer did not receive taxable income.

6. The taxpayer in support of his appeal, relies upon the following proposition of law:

Any earnings or profits accumulated or increase of value of property acquired before March 1, 1913, may be distributed, exempt from tax.

Taxpayer respectfully prays that this Board may hear and determine his appeal.

(s) CAMDEN R. McATEE,
Counsel for Taxpayer.
MDH

State of West Virginia,
County of , ss:

D. J. F. STROTHER, being duly sworn, states that he has read the foregoing petition, and is familiar with the statements therein contained, and that the facts therein stated are true, except such facts as are stated to be upon information and belief, and those facts he believes to be true.

(s) D. J. F. STROTHER.

Subscribed and sworn to before me this 23rd day of December, 1925.

(s) RUBY SLEDGE REYBURN,
(SEAL) Notary Public.

(Commissioned as Ruby Sledge).

(10) Form NP-2

TREASURY DEPARTMENT

(COPY) WASHINGTON

Nov. 9, 1925.

IT:PA:1,
KB-107-60D

Mr. D. J. F. Strother,
Welch, West Virginia.

Sir:

A reaudit of your 1919, 1920 and 1921 income tax returns in connection with the information contained in the report of the Internal Revenue Agent in Charge at Huntington, West Virginia, dated May 10, 1924, together with the data subsequently submitted through correspondence and in conference, and in the recommendation of the Solicitor of Internal Revenue based upon consideration thereof, discloses deficiencies in tax aggregating $3,268.-12, as shown in the attached statement.

In accordance with the provisions of Section 274 of the Revenue Act of 1924, you are allowed 60 days from the date of mailing of this letter within which to file an appeal to the United States Board of Tax Appeals contesting in whole or in part the correctness of this determination.

Where a taxpayer has been given an opportunity to appeal to the United States Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has appealed and an assessment in accordance with the final decision on such appeal has been made, no claim in abatement in respect of any part of the deficiency will be entertained.

If you acquiesce in this determination and do not desire to file an appeal, you are requested to sign the in-

closed agreement consenting to the assessment of the deficiency and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:PA:1-KB-107-60D. In the event that you acquiesce in a part of the determination, the agreement should be executed with respect to the items agreed to.

Respectfully,

D. H. BLAIR,
Commissioner.
By (s) C. R. NASH,
Assistant to Commissioner.

Inclosures:
Statements
Agreement—Form A

(COPY) Nov 9, 1925.

IT:PA:1
KB-107-60D

(11) STATEMENT

In re:
Mr. D. J. F. Strother,
Welch, West Virginia:

Year	Deficiency in Tax
1919	$ 963.62 (Waiver)
1920	1,181.02
1921	1,123.48
Total	$3,268.12

The report of the Internal Revenue Agent in Charge at Huntingdon, West Virginia, dated May 10, 1924, has been reviewed and approved by this office.

Due consideration has been given to the information recently submitted in substantiation of your contention relative to the taxability of dividends paid upon shares

of stock assigned to your wife. However, your contention has been denied for the reason that the conditions of the assignment in question operate to defeat the legal right to make an assignment, in that the control and disposition of the income remains at your discretion. This conclusion is based upon consideration of the following statements contained in your affidavit of September 17, 1925.

The assignment and endorsement of the certificates to the wife were made: "With the understanding that the assignee was to have and receive from the assigned stock so much of its returns as together with any other receipts by her would not exceed stock non-taxable to her, and the remaining returns from the stock would and should belong to the affiant.

It is held, therefore, that there has been in effect an assignment of income and not an assignment of principal which the unit has ignored in all cases in which this feature was existent.

All information in substantiation of your contention that the dividends paid by the Bankers Pocahontas Coal Company, during the years 1919, 1920 and 1921 represented a return of capital, therefore non-taxable, has been considered by the Solicitor of Internal Revenue who recommended that the action previously taken by the Income Tax Unit in this matter be sustained for the reason that this Company's earnings since March 1, 1913, were in excess of the dividends paid since that date.

Your wife's returns for the years 1920 and 1921 will (12) be adjusted to give effect to the dividends reported on your returns which have now been considered as taxable income to you, as explained above. No adjustment will be made for the year 1919 on account of the operation of the Statute of Limitations.

Payment should not be made until a bill is received from the Collector of Internal Revenue for your district, and remittance should then be made to him.

ANSWER

(13) Filed Jan. 21, 1926.

UNITED STATES BOARD OF TAX APPEALS

Appeal of

D. J. F. Strother, Welch, West Virginia. Docket No. 10472.

The Commissioner of Internal Revenue by his attorney, A. W. Gregg, Solicitor of Internal Revenue, for answer to the petition of the above-named taxpayer admits, denies and alleges as follows:

(1) Admits the allegations contained in paragraphs 1, 2 and 3 of the taxpayer's petition.

(2) Denies that any errors have been committed in the determination of the deficiency set forth in the deficiency letter.

(3) Admits that the Commissioner has added to taxpayer's income for the years 1919, 1920 and 1921 the amounts indicated in paragraph 4(a) of the taxpayer's petition, but denies that such action is erroneous.

(4) Denies, generally and specifically, each and every allegation contained in the taxpayer's petition not hereinbefore admitted, qualified or denied.

PROPOSITION OF LAW

The dividends received by the taxpayer in the amounts and for the years indicated in paragraph 3 of this answer from the Bankers Pocahontas Coal Company out of earnings of such company from its leases of its coal lands executed prior to March 1, 1913, are income within the meaning of Section 213 of the Revenue Acts of 1918 and
(14) 1921 and are not a return of capital as alleged by the taxpayer.

WHEREFORE, it is prayed that the taxpayer's appeal be denied.

A. W. GREGG,
Solicitor of Internal Revenue,
Attorney for Commissioner of
Internal Revenue.

Of Counsel:

ELLIS W. MANNING,
Special Attorney,
Bureau of Internal Revenue.

(15) **STATEMENT**

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

v. Docket No. 25275.

Commissioner of Internal Revenue,
Respondent.

The petition and answer are in substance the same as in Docket 10472 and addressed to the same issues herein against adjustments and deficiencies for the calendar years 1922 and 1923, and same are here omitted excepting Paragraphs (b) and (c) of said petition, and the deficiency letter which are as follows:

(b) That respondent Commissioner has ruled that the relation of lessor and lessee existed between said Bankers Pocahontas Coal Company and its operating companies and has allowed to said lessor a depletion rate of .036 per unit, and which allowance was available to said corporation as a deduction in the computation of (16) its taxable net income. That said corporation is not engaged in business, and only receives and makes distribution of payments under the contracts with operating companies aforesaid, and on receipt thereof, distributes same to its stockholders, including this taxpayer, without retaining any part of said receipts. That

thereby in the distributions received by taxpayer in the years 1922 and 1923 was included the depletion allowance to said corporation as non-taxable income and that same is non-taxable when received by this taxpayer, being distribution of a depletion reserve.

(c) That the depletion unit of .036 per unit, allowed by the respondent Commissioner, is erroneous and not a sufficient return of capital interest of said corpora-
(17) tion.

COPY Docket No. 25275.

TREASURY DEPARTMENT

WASHINGTON

IT:PA:4-60D Feb. 26, 1927.
FAL

Mr. D. J. F. Strother,
Welch, West Virginia.

Sir:

An audit of your income tax returns for the years 1922 and 1923, in connection with an examination of your books of account and records discloses an aggregate deficiency in tax amounting to $4,366.82. This deficiency is the result of certain adjustments which are shown in the attached statement.

In accordance with the provisions of Section 274 of the Revenue Act of 1926, you are allowed 60 days from the date of mailing of this letter within which to file a petition for the redetermination of this deficiency. Any such petition must be addressed to the United States Board of Tax Appeals, Earle Building, Washington, D. C., and must be mailed in time to reach the Board within the 60-day period, not counting Sunday as the sixtieth day.

Where a taxpayer has been given an opportunity to file a petition with the United States Board of Tax Appeals and has not done so within the 60 days prescribed

and an assessment has been made, or where a taxpayer has filed a petition and an assessment in accordance with the final decision on such petition has been made, the unpaid amount of the assessment must be paid upon notice and demand from the Collector of Internal Revenue. No claim for abatement can be entertained.

If you acquiesce in this determination and do not desire to file a petition with the United States Board of Tax Appeals, you are requested to execute a waiver of your right to file a petition with the United States Board of Tax Appeals on the inclosed Form A, and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:PA:4-60D-FAL. In the event that you acquisce in a part of the determination, the waiver should be executed with respect to the items to which you agree.

Respectfully,

D. H. BLAIR,
Commissioner.
By (Signed) C. R. NASH,
Assistant to the Commissioner.

Inclosures:
Statement
Form A
Form 882.

(18) STATEMENT

IT:PA:4-60D
FAL

Feb. 26, 1927.

In re:

Mr. D. J. F. Strother,
Welch, West Virginia.

Year	Deficiency in Tax
1922	$2,549.05
1923	1,817.77
Total	$4,366.82

The report of the Internal Revenue Agent in Charge at Huntington, West Virginia, dated June 1, 1926, a copy of which was furnished you, has been reviewed and approved by this office as submitted.

You are advised that consideration has been given to your letter of protest dated August 6, 1926, submitted to the Internal Revenue Agent relative to the inclusion in income of dividends received from the Bankers Pocahontas Coal Company but the information submitted is not sufficient to warrant a change in the adjustment as recommended by the agent.

Payment of the tax should not be made until a bill is received from the Collector of Internal Revenue for your district, and remittance should then be made to him.

(19) PRELIMINARY STATEMENT

Index:

Pages covered: 4

Schedules 1 to 4 inclusive.

SUMMARY

Year	Additional Tax
1922	$2,549.05
1923	1,817.77
Total	$4,366.82

Additional tax is due to taxpayer's elimination of dividends of the Bankers Poca. Coal Company. The reason for elimination of dividends is fully explained in previous revenue agent's report of April 24, 1924 and the upholding of his action by the Unit in letter of December 6, 1924. Therefore, same have been added to income for years under examination.

(20) Schedule 1

Year 1922

Net Income

Net income as disclosed by return		$28,293.09
As corrected		44,421.09
Net adjustment		$16,128.00
Unallowable deductions and additional income:		
(a) Dividends	$16,128.00	
Net adjustment as above		$16,128.00

Schedule 1-A

Explanation of Items

(a) Item #7. Dividends reported	$ 2,044.00
Dividends omitted, Bankers Pocahontas Coal Company	16,128.00
Dividends as corrected	$18,172.00

(21) Schedule 2

Year 1922

Computation of Tax

Total net income, (See Schedule 1)		$44,421.09
Income subject to surtax		$44,421.09
Less:		
Exemption	$2,000.00	
Dividends	18,172.00	
Balance		20,172.00
Income subject to normal tax		$24,249.09

Tax at 4% on $4,000.00	$ 160.00	
Tax at 8% on $20,249.09	1,619.93	
Surtax, husband's income	3,784.22	
Total tax		$ 5,564.15
Total tax assessable		5,564.15
Tax previously assessed		3,015.10
Additional to be assessed		$2,549.05

Schedule 3

Year 1923

Net Income

Net income as disclosed by return		$32,787.00
As corrected		46,675.00
Net adjustment		$13,888.00
Unallowable deductions and additional income:		
(a) Dividends	$13,888.00	
Net adjustment as above		$13,888.00

Schedule 3-A

(22) Year 1923

Explanation of Items

(a) Item #7.	
Dividends reported	$ 3,524.00
Dividends omitted, Bankers Pocahontas Coal Company	13,888.00
Dividends as corrected	$17,412.00

Schedule 4

Year 1923.

Computation of Tax

Total net income		$46,675.00
Income subject to surtax		$46,675.00
Less:		
Exemption	$ 2,000.00	
Dividends	17,412.00	
Balance		19,412.00
Income subject to normal tax		$27,263.00
Tax at 4% on $4,000.00	$ 160.00	
Tax at 8% on $23,263.00	1,861.04	
Surtax, husband's income	4,241.75	
Total tax assessable		$6,262.79
Less:		
Credit of 25% per Section 1200, Revenue Act of 1924	$ 1,565.70	
		1,565.70
Net tax assessable		$ 4,697.09
Total tax previously assessed before deducting any credits	$ 3,839.09	
Less:		
Credit of 25% per Section 1200, Revenue Act of 1924	959.77	
Net tax previously assessed		2,879.32
Additional to be assessed		$ 1,817.77

drs-5

(23) **STATEMENT**

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

v. Docket No. 32170.

Commissioner of Internal Revenue,
Respondent.

The petition and answer are in substance the same as in Docket 25275 and addressed to the same issues herein against the adjustments and deficiencies for the calendar years 1924 and 1925, and same are here omitted excepting the deficiency letter, which is as follows:

(24) Docket No. 32170

"EXHIBIT A"

TREASURY DEPARTMENT

WASHINGTON

Office of
Commissioner of Internal Revenue. Oct. 5, 1927.

IT:FAR:C-6
MB-60D

Mr. D. J. F. Strother,
Welch, West Virginia.

Sir:

The determination of your income tax liability for the taxable years 1924 and 1925 as set forth in office letter dated September 12, 1927, discloses an aggregate deficiency in tax of $1,239.56 as shown in the attached statement.

In accordance with the provisions of Section 274 of

the Revenue Act of 1926, you are allowed 60 days from the date of mailing of this letter within which to file a petition for the redetermination of this deficiency. Any such petition must be addressed to the United States Board of Tax Appeals, Earle Building, Washington, D. C., and must be mailed in time to reach the Board within the 60-day period, not counting Sunday as the sixtieth day.

Where a taxpayer has been given an opportunity to file a petition with the United States Board of Tax Appeals and has not done so within the 60 days prescribed and an assessment has been made, or where a taxpayer has filed a petition and an assessment in accordance with the final decision on such petition has been made, the unpaid amount of the assessment must be paid upon notice and demand from the Collector of Internal Revenue. No claim for abatement can be entertained.

If you acquiesce in this determination and do not desire to file a petition with the United States Board of Tax Appeals, you are requested to execute a waiver of your right to file a petition with the United States Board of Tax Appeals on the inclosed Form A, and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:FAR:C-6-MB* 60D. In the event that you acquiesce in a part of the determination, the waiver should be executed with respect to the items to which you agree.

Respectfully,

(s) D. H. BLAIR,
Commissioner.
By (s) C. R. NASH,
Assistant to the Commissioner.

Inclosures:
Statement
Form A
Form 882

(25) STATEMENT

IT:FAR:C-6
MB-60D

Oct. 5, 1927.

In re:
Mr. D. J. F. Strother,
Welch, West Virginia.

Year	Deficiency
1924	$ 95.09
1925	1,144.47
Total	$1,239.56

The report of the Internal Revenue Agent in Charge at Huntington, West Virginia dated May 28, 1927, transmitted to this office August 18, 1927, covering an examination of your income tax returns for the years 1924 and 1925 has been reviewed in this office in connection with your protests dated July 20, 1927, and September 16, 1927.

Synopsis of your returns as corrected follow:

1924

Net income reported on return			$18,274.00
Add:			
1. Partnership profits		$ .33	
2. Dividends		16,400.00	
3. Profit on real estate		500.00	
		$16,900.33	
Deduct:			
4. Taxes	$ 55.77		
5. Contribution increased	23.80		
6. Other deduction ($15,000.00 loss in South Fork Coal Company increased to $23,184.00)	8184.00	8,263.57	8,636.76
Adjusted net income			$26,910.76

Explanation of Changes

1. Distributive share of income from the partnership Strother Sale, Curd and Tucker, Welch, West Virginia, (26) increased from $23,883.00 to $23,883.33 to agree with amount shown in report covering examination of return filed by the partnership.

2. Dividends of $16,400.00 received from Bankers Pocahontas Coal Company included as taxable income. Your protest dated September 16, 1927, in which you state that the same issue in prior years is pending a decision of the Board of Tax Appeals has been considered. However, it is necessary to proceed with your case in the usual manner since it cannot be held pending such decision.

3. Profit from sale of real estate which was omitted is included in taxable income.

4. and 5. Amounts checked from your records.

6. In view of information presented in conference August 15, 1927, in the office of the Internal Revenue Agent in Charge Huntington, West Virginia, the entire amount invested in stock of the South Fork Coal Company, $23,184.00 instead of $15,000.00 is considered a loss and allowed. Formal dissolution of the corporation was not considered a requisite in this instance, since it was evident that the stockholders would receive nothing in liquidation.

1925

Net income reported, Line 19		$30,437.00
Add:		
1. Interest	$ 0.31	
2. Partnership income	.68	
3. Dividends	11,920.00	
4. Taxes	9.11	
	$11,930.10	
Deduct:		
5. Contributions	9.08	11,921.02
Adjusted net income		$42,358.02

Explanation of Changes.

1, 4, and 5 checked with records.

2. Distributive share of income from the partnership (27) Strother. Sale, Curd and Tucker increased from $20,960.00 to $20,960.68.

3. See Number 2 of the year 1924 for explanation.

Payment of the tax should not be made until a bill is received from the Collector of Internal Revenue for your district and remittance should then be made to him.

FINDINGS OF FACT AND OPINION

(28) 18 B. T. A. ----------

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Co.,
Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 10472, 14516, 14517, 25275, 32170, 42664. Promulgated January 22, 1930.

Royalties received under leases of coal lands are held to constitute gross income and not proceeds from the sale of coal in place.

Money received in compromise of a suit to recover the value of coal extracted by a trespasser, plus damages to the property held, on the record, to constitute taxable income.

Proper depletion rate per ton of coal mined determined.

Camden R. McAtee, Esq., and Wells Goodykoontz, Esq., for the petitioners. M. E. McDowell, Esq., and Frank B. Schlosser, Esq., for the respondent.

These proceedings, consolidated for hearing and de-
(29) cision, involve deficiencies as follows:

Docket No.		
14517	1920	$6,797.56
14516	1921	7,871.64
	1922	4,149.24
	1923	4,113.67
42664	1924	3,362.17
	1925	6,419.04
	1926	7,138.67
10472	1919	863.62
	1920	1,181.02
	1921	1,123.48
25275	1922	2,549.05
	1923	1,817.77
32170	1924	95.09
	1925	1,144.47

In the petitions of Bankers Pocahontas Coal Co. (Docket Nos. 14517, 14516, and 42664), the first contention made is that there is no tax due, upon the ground that the amounts received by the petitioner during the taxable years represented installment payments upon the sales of coal in place, which coal had been sold prior to March 1, 1913.

The second contention is that if the Bankers Pocahontas Coal Co. is to be considered as a lessor, then the amount of depletion which has been allowed to that company has been erroneously computed by the respondent.

For the year 1920, there are two incidental questions which simply amount to the inclusion in 1920 of income which was previously reported for 1919. For 1924, there is an incidental question arising by reason of damages received by the petitioner, the contention being that the (30) amount received as damages to property is not properly includable in gross income.

The contentions in the petitions of D. J. F. Strother (Docket Nos. 10472, 25275, and 32170) are:

(1) That the petitioner received no taxable income when he received distributions from Bankers Pocahontas Coal Co., claimed by the petitioner to be tax-exempt by reason of being distributions of a part of the capital of that company;

(2) That the depreciation rate properly allowable to the Bankers Pocahontas Coal Co., if not properly allowed, has distorted his income;

(3) That the Bankers Pocahontas Coal Co., has made distribution each year of all of its revenues derived from its contracts; that it has accordingly distributed its depletion reserve and that the petitioner should be entitled to an allowance for that depletion reserve in the computation of dividends received from it.

FINDINGS OF FACT

In July, 1912, the Bankers Pocahontas Coal Co., a West Virginia corporation (hereinafter sometimes called the corporation), acquired the fee simple title to approximately 6,200 acres of coal lands, including both the surface and the mineral rights in the State of West Virginia. The land had no appreciable value except for the coal (31) content.

Upon incorporation in 1912, the corporation acquired by formal assignment and has continued to retain the beneficial interest of the original owners in certain contracts affecting the coal content which were executed in 1901 and 1902 with various operating companies and to which contracts the 6,200 acres and coal content were subject.

These contracts were originally prepared by D. J. F. Strother, who at that time was attorney, director, and stockholder in the predecessor corporations. The form of the contracts is that prevailing in the West Virginia coal fields, which followed the Pennsylvania form of contracts as introduced by Pennsylvanians who were largely instrumental in the early coal development in the West Virginia field.

By agreement of parties a copy of such contracts was offered and received in evidence as typical of the several contracts existing on the acreage acquired by the corporation in 1912. The specimen contract provides in part as follows:

This contract of lease, made this 17th day of June, 1901, between the Tug River Coal Land Company, a corporation, authorized and doing business under and by virtue of the laws of the State of West Virginia, party of the first part, hereinafter called the Lessor, and the Cletus Coal and Coke Company, a like corporation, hereinafter called the Lessees.

Witnesseth: First: That in consideration of the terms, conditions and stipulations hereinafter set forth to be performed and observed by the lessees, the Lessor doth demise, let and lease for coal mining and coal coke-ing purposes only, to the lessee, for the period of thirty (30) years, from the 1st day of January, 1901, a certain tract of land situate, lying and being in the County of McDowell and State of West Virginia, on the waters of Tug River containing eight hundred acres, more or less (32) and bounded and described as follows: (Description omitted.)

The Lessor covenants to and with the said Lessee that

it has good right and title to said land, and that the said Lessee shall have quiet, and peaceable enjoyment of the same during the continuance of this lease.

SECOND: The Lessees shall have the sole and exclusive privilege of mining and coking coal on the above described premises and of conducting a general mercantile business thereon during the continuance of this lease, and the privilege of using so much of the surface of said land and so much of the timber, stone, sand, clay and water as may be necessary for the mining, coking and building purposes of said Lessees, but for no other purpose.

* * * * * * *

THIRD: In consideration thereof, the Lessees hereby covenant and agree to pay to the Lessor, its successors and assigns, during the continuance of this lease, as rental for the said premises, the following royalties, to-wit: Ten (10) cents per ton for each and every ton of 2240 pounds of coal mined, dug, carried away from or sold or used on the said premises for any other purpose than the manufacture of coke; and fifteen (15) cents for each and every ton of 2240 pounds of coke manufactured upon the said premises, and sold thereon or therefrom. * * *

* * * * * * *

SEVENTH: The Lessees agree and bind themselves to pay to the Lessors the sum of three thousand dollars for the first year, dating from the 1st day of November, 1901, and the sum of five thousand dollars for each and every year thereafter, during the continuance of this lease, as a minimum rental or royalty for the property herein demised, whether the quantity of coal mined and coke manufactured shall produce that amount of royalty or not, but the Lessees shall have the privilege of mining the next succeeding year, free of royalty, a sufficient amount of coal above the amount necessary to produce the minimum royalty for that year to reimburse themselves for the deficiency in the preceding year. * * *

* * * * * * *

NINTH: The Lessees agree to pay all the taxes that

(33) may be assessed against the demised property and the improvements thereon, or upon the coal mined or coke manufactured, during the continuance of this lease, all other assessments by operation of law whatsoever, when and as the same may become due.

* * * * * * * *

ELEVENTH: At the termination of this lease, otherwise than by forfeiture. all the improvements placed upon the said surface of the demised premises, by the Lessees, shall be valued by two disinterested persons, one to be chosen by each of the parties hereto, and in case of their disagreement, these two shall choose a third, and the persons thus chosen shall value said improvements, and the Lessor shall have the privilege of purchasing said improvements at such valuation, within thirty (30) days after notice thereof. If the Lessor shall not, within said thirty days, accept said improvements, at such valuation, the Lessees shall have the privilege of removing the same from the leased premises within the period of ninety days from the expiration of said thirty days.

TWELFTH: The Lessees shall have the right to at the expiration of the said thirty years, renew this lease, with the terms, stipulations and agreements as herein set forth, provided that they shall have complied with and performed all the conditions, covenants, agreements and stipulations to be *by* them complied with or performed.

THIRTEENTH: It is hereby mutually understood and agreed that the covenants, agreements, stipulations herein contained to be performed by the one party or the other, shall be binding on the parties hereto, their successors and assigns.

IN WITNESS WHEREOF, the parties hereto have caused these presents to be signed in their corporate names by their respective presidents, and their corporate seals to be hereunto affixed as of the day and year first above written.

All of these agreements were in the main, with the

exception as to minor and non-essential provisions, the
(34) same as the sample agreement set forth above as the Cletus lease.

From time to time these agreements were reassigned by the lessees to new and different operating lessees, largely with the permission of the lessor corporation.

The cost to the corporation of the properties acquired by it was between $407,000 and $507,000.

The contracts on the property on March 1, 1913, are shown by the following:

SCHEDULE 1

CONTRACTS ON MARCH 1, 1913.

Lessee at 3/1/13	Approximate Acreage	Royalty per ton	Minimum Royalty per annum
Lease			
#1 Vaughan Coal & Coke Co.	1000	8c	$5,000
#2 Superior Pocahontas Coal Co.	1200	10c	5,000
#3 New Pocahontas Coal Co.	1300	7c	4,000
#4 Oregon Coal & Coke Co.	2000	10c	10,000
#5 Pocahontas Smokeless Coal Co.	600	5c	None
#6 J. B. B. Coal Co.	100	1c(haulage)	300

The estimated recoverable tonnage on March 1, 1913,
(35) is shown by the following:

SCHEDULE 2

ESTIMATED RECOVERABLE TONNAGE ON MARCH 1, 1913

Lease #1 Vaughan Coal & Coke Co.	2,416,452

Lease #2	Superior Pocahontas Coal Co.	2,309,444	
Lease #3	New Pocahontas Coal & Coke Co.	3,773,835	
Lease #4	Oregon Coal & Coke Co.	4,906,902	upper or Welch Seam
		22,765,666	lower seam
Lease #5	Pocahontas Smokeless Coal Co.	493,172	
Lease #6	J. B. B. Coal Co.	943,171	
	Total	37,608,642	

The tonnage mined and royalty receipts of the corporation for the years 1913 to 1919, inclusive, is shown by leases as follows:

	Tonnage mined	Royalty Receipts
Lease No. 1	393,379	34,497.20
Lease No. 2	528,255	61,263.41
Lease No. 3	571,502	52,352.49
Lease No. 4	472,980	77,465.45
Lease No. 5	250,601	11,874.92
Lease No. 6	664,991	6,641.15
Total	2,881,708	244,094.62

The tonnage mined, the tonnage paid for, and the royalty receipts for the taxable years involved in these pro-
(36) ceedings are shown by the following:

Lease No. 1—Fall River Pocahontas Collieries Co.

Year	Tonnage mined	Paid for	Receipts
1920	71,594	71,593	5,727.48
1921	98,587	98,587	7,886.98
1922	85,132	85,132	6,810.55
1923	81,373	81,373	6,509.88
1924	95,859	85,859	7,668.72
1925	81,552	81,557	6,524.16
1926	90,764	90,765	7,261.12

Lease No. 2—Superior Pocahontas Coal Co.—Cletus Mine

Year	Tonnage mined	Paid for	Receipts
1920	57,189	120,000	12,000
1921	54,660	120,000	12,000
1922	55,864	120,000	12,000
1923	51,422	120,000	12,000
1924	57,928	120,000	12,000
1925	68,804	120,000	12,000
1926	90,029	120,000	12,000

Lease No. 3—W. E. Deegans (Later New Pocahontas Coal Co. and Monarch Smokeless Coal Co.)

Year	Tonnage mined	Paid for	Royalty rate	Receipts
1920	113,086	113,686	.07	8,372.78
1921	92,983	104,695	.07	7,916.02
1922	141,895	141,895	.07	7,328.66
1923	131,961	131,961	.08	10,556.83
1924	160,428	160,440	.08	12,835.26
1925	151,694	151,619	.08	12,135.57
1926	166,280	164,533	.08	13,162.70

Lease No. 4—Oregon Coal Company (Later Solvay Collieries Company and Kingston Pocahontas Coal
(37) Company).

WARWICK MINE

Year	Tonnage mined	Paid for	Receipts
1920	86,918	100,000	10,000.00
1921	15,297	100,000	10,000.00
1922	109,853	100,002	10,000.02
1923	113,565	113,659	11,365.72
1924	125,811	125,811	12,581.10
1925	91,170	100,000	10,000.00
1926	118,273	118,827	11,827.70

Lease No. 4—Solvay Collieries Company (Later Kingston Pocahontas Coal Co.)

EXETER MINE

Year	Tonnage mined	Paid for	Receipts
1920	19,231	187,500	18,750.00
1921	25,024	306,250	30,625.00
1922	45,483	370,433	37,043.38
1923	74,152	340,782	34,078.20
1924	103,877	343,657	34,365.70
1925	117,792	325,000	32,500.00
1926	153,717	335,115	33,511.56

Lease No. 5—Pocahontas Smokeless Coal Company (Later Central Pocahontas Coal Company.)

Year	Tonnage mined	Paid for	Receipts
1920	27,671	25,758	1,287.88
1921	5,622	4,111	205.57
1922	8,611	8,773	438.65
1923 (Jan.1-Mch.31)	3,877	3,877	193.85

(38) Lease No. 6—Hensley Coal Company (Later known successively as J. B. B. Coal Company, Dexcar Pocahontas Coal Company and Fordson Coal Co.) The payment of 1c per ton ($300.00) minimum per year, is a haulage fee for use of an easement over Bankers Pocahontas property to coal mined on other properties by the operators.

Year	Tonnage mined	Paid for	Receipts
1920	80,506	80,506	805.06
1921	38,990	6,827	68.27
1922	19,811	-----	-----
1923	20,811	15,771	157.71
1924	12,025	12,025	120.25
1925	12,640	12,640	126.40
1926	7,258	51,822	518.22

In the several taxable years in controversy the corporation was upon a cash receipts and disbursements basis of accounting and its income, except minor items not in controversy, consisted of payments received under the several contracts from the various operating companies, and income and profits-tax returns were filed for each of the taxable years and thereafter audited by the Commissioner resulting in the deficiency notice forming the basis of the present proceedings.

In computing the deficiencies the Commissioner considered the relation of the corporation and the operating companies to be that of lessor and lessee and allowed the corporation a depletion deduction of $0.036 per ton mined for the years 1920 to 1926, inclusive, the same depletion rate as was allowed by the Commissioner for 1919 and prior years.

For prior years 1914 to 1919, inclusive, the Commissioner proposed additional taxes in the amount of $6,267.08 and required the corporation to pay same, which (39) thereafter brought an action on February 17, 1923, in the United States Court for the Southern District of West Virginia against the collector to recover same on the grounds that payments under said contracts received by the corporation were the proceeds of a sale of coal in place consummated before March 1, 1913, or of choses in action existing on said date, or that petitioner plaintiff, as a lessor, was entitled to a unit depletion rate of not less than $0.05 per ton mined in the computation of net taxable income, and consequently said taxes were erroneously and illegally assessed and collected. The issues were made in said action, and same were submitted for judgment upon the evidence adduced by the parties, and were decided by opinion of the court and judgment entered thereon that petitioner plaintiff in the computation of said taxes was entitled to a depletion unit of $0.05 per ton instead of $0.036 computed by the Commissioner. A recovery of $5,373.01 from said collector by petitioner plaintiff was adjudged and said judgment was duly paid by the United States. In said action the Bankers Pocahontas Coal Co., one of the petitioners herein, was plaintiff; plaintiff petitioner appearing in its own right and the

collector as defendant, who was defended in said action by the United States District Attorney and the Solicitor of Internal Revenue (now General Counsel). In this proceeding and in said court action the subject matter of the action and of these proceedings is the same, namely, the depletion unit allowable in computing the amount of such depletion deduction as will return to the taxpayer the capital value existing in the coal content of the corpora-
(40) tion's property as of March 1, 1913.

In his computation of invested capital of the corporation for the calendar year 1920 in the deficiency appealed from herein, the Commissioner used the tax computation determined in said action as due and owing for the calendar year 1919, which was based upon the allowance of a $0.05 depletion rate for 1919. In the years subsequent to 1919, the Commissioner has applied the depletion rate of $0.036 per ton. The court action was instituted February 17, 1923, and the judgment therein was entered January 31, 1928. The deficiency letters were mailed for 1920 on February 15, 1926; for 1921, 1922, and 1923 on February 12, 1926; for 1924, 1925, and 1926 on January 15, 1929. Before the issue of the last named deficiency notice the attention of the Commissioner was specifically called to the pendency and decision of the court action.

In the several taxable years, and particularly in 1919, the corporation received its contract payments each month and same when received were about thirty days overdue. The payment for December was consistently reported in the year's receipts, although same did not come to hand until January. In December, 1919, the corporation received a tax refund of $180, which it put on its books in January, 1920, and likewise received a contract payment of $5,434.66. These amounts were reported as income for 1919 and the Commissioner has included same again as 1920 income, as shown by the books to have been received in the latter year.

In 1920, the Flanagan Coal Co., which owned land ad-
(41) jacent to the petitioner corporation, trespassed on the land of the petitioner corporation and removed coal to which it had no right. It then destroyed the entries so that the damage or extent of the operation

could not be determined. The corporation discovered the situation in 1923 and brought suit for damages and, as a result of a compromise of the suit, received in 1924, $3,770.40 in settlement and adjustment of the controversy. The petitioner corporation had no contractual relation with the trespasser and the settlement had no relation to the coal extracted, as the amount of same could not be determined. The Commissioner held the damages received were equivalent to a royalty and adjusted same by the allowance of $0.036 per ton as depletion on 15,000 tons estimated to have been damaged or removed by the trespasser.

In the several years involved herein the petitioner, Strother, as one of the corporation's stockholders, received payments from the Bankers Pocahontas Coal Co. and reported same in his returns but did not return them as taxable income. The corporation received said amounts from its operating contracts and entirely distributed them, including any depletion reserve. No allowance was made by the Commissioner to the petitioner, Strother, for any depletion reserve received by him and the Commissioner added the entire receipts to his net income and has determined deficiencies accordingly.

OPINION

Smith: In these proceedings the Bankers Pocahontas (42) Coal Co. contends that it received no income during the taxable years and all of the moneys received as royalties were in part payment of coal in place which had been sold prior to March 1, 1913; that the typical contract quoted in part in the findings of fact constituted a sale of coal in place made before March 1, 1913, under the laws of West Virginia, and that on March 1, 1913, the petitioner held only a chose in action from which no taxable income was subsequently received; that leasing agreements similar to those involved in these proceedings have been held by the courts of Pennsylvania in Delaware & Hudson Canal Co. v. Hughes, 183 Pa. 66; 38 L. R. A. 826; Lehigh & Wilkesbarre Coal Co. v. Wright, 177 Pa. 387, 35 Atl. 919; Denniston v. Haddock, 200 Pa. 426, 50 Atl. 197; and by the courts of West Virginia in Wallace v.

Elm Grove Coal Co., 58 W. Va. 449, 52 S. E. 485; National Coal Co. v. Overholt, 94 S. E. 735 (W. Va.); to constitute sales of coal in place; that the Board is bound to give the same effect to such leasing agreements as has been given to them by the courts of the States of Pennsylvania and West Virginia.

This is the same contention as has been made before the Board in many different cases. Beginning with the case of Nelson Land & Coal Co., 3 B. T. A. 315, and following down through a number of decisions, this Board (43) has uniformly held that sums received as bonus or royalties from leases of oil and mineral rights were not income from the sale or exchange of capital assets, but constituted a part of the gross income that the petitioner was obligated to return as a part of its gross income. It is likewise the same contention which was made before the District Court of the United States for the Southern District of West Virginia in the case of Bankers Pocahontas Coal Co. v. Albert B. White, referred to in our findings, which was a suit for the recovery of additional taxes paid for the years 1914 to 1919. The learned judge of that court disposed of that case in the following language:

This brings on the first contention of the plaintiff, that is, that the plaintiff, by the reserved rentals and royalties, is being paid for the land and the coal thereunder, and that such rentals and royalties are not "income" but "purchase money."

Personally, I believe this statement to be true, but I cannot, in the face of all the decisions, sustain it here.

I therefore hold, that the royalty payments are income, and should pay a tax as such.

Judicial decisions upon the point are many. See Hirschi v. United States, Ct. Cl. , decided May 6, 1929; Berg v. Commissioner, 33 Fed. (2d) 641, certiorari denied 50 S. Ct. 69; Stanton v. Baltic Mining Co., 240 U. S. 103; Von Baumbach v. Sargent Land Co., 242 U. S. 503; United States v. Biwabik Mining Co., 247 U. S. 116. In Hirschi v. United States, supra, the court stated:

The one question involved is whether the income re-
(44) ceived by the plaintiff from said lease is taxable as income from the sale of capital assets or his ordinary income. If it is from the sale of capital assets the plaintiff is entitled to a refund; if it is not, he is not so entitled. Since the decision in Stratton's Independence v. Howbert, 231 U. S. 399, following through Stanton v. Baltic Mining Co., 240 U. S. 103; Von Baumbach v. Sargent Land Co., 242 U. S. 503; United States v. Biwabik Mining Co., 247 U. S. 116, it has been consistently held that the trustees received from such leases of oil and mineral lands were to be treated as gross income. The principle is too well established to require extended discussion.

* * * * * * * * * *

The Federal Government is not limited in its selection of subjects for taxation by the construction of the State courts as to the property rights of individuals, provided the subject taxed was primarily a proper subject for taxation. Congress in passing a revenue act does not, and is not called upon to suit the revenue system of the country to the varying and conflicting decisions and laws of the different states. A revenue act is an act of Congress passed in the exercise of its constitutional right, and therefore the supreme law of the land, and where the constitutional powers of the Federal Government and the States conflict those of the States must give way.

Petition for writ of certiorari was denied by the Supreme Court in this case on October 21, 1929.

In Van Devender, 8 B. T. A. 697, contracts in West Virginia made by the petitioner and others from the mining of coal were held to constitute leasing agreements upon the authority of Henry L. Berg and Wife, 6 B. T. A. 1287, and Rosenberger v. McCaughn, 20 Fed. (2d) 139. Counsel for the petitioners suggest, however, that in the Van Devender case the petitioner made the contracts and
(45) that they were not transferred to third parties; that the instant proceedings present the case of such transfer and that if there is any income received from

the contract subject to tax it is ascertained by the exclusion of all capital from same, according to the final decision of Rosenberger v. McCaughn, 25 Fed. (2d) 699. We see no justification for the distinction sought to be made. The Bankers Pocahontas Coal Co. received its property in July, 1912, subject to certain leases upon the property. In our opinion the corporation simply stands in the shoes of the original lessors. The royalties received by it constitute part of its gross income. From such income it is entitled to deduct a reasonable amount for the depletion of its property during the taxable years.

In computing the deficiencies for the years 1920 to 1926, the respondent has used a depletion rate of $0.036 per ton of ore mined each year. The respondent held that this was a reasonable depletion rate and that such rate multiplied by the tons mined each year constituted a reasonable deduction for depletion. The corporation taxpayer contends that this is not a proper rate and that its application does not permit the deduction of a reasonable amount for depletion. In support of its contention it submits the decision of the District Court made in the above cited case of Bankers Pocahontas Coal Co. v. Albert B. White, in which the court found that a reasonable depletion rate was five cents per ton multiplied by the number of tons of ore mined during each taxable (46) year. The evidence before the District Court was introduced before the Board and in addition much additional evidence showing the cost of the properties to the Bankers Pocahontas Coal Co. at the time they were acquired in 1912, and likewise the agreed estimated tonnages in each of the leases upon the land. With respect to the cost of the properties to the petitioner corporation D. J. F. Strother, the president of the corporation, testified as follows:

My recollection is that a bond issue outstanding on the property at that time was either two hundred and forty, or two hundred and sixty thousand dollars; I know I am right in either one amount or the other; we paid out sixty thousand dollars in cash; there were some troubles with the title and we paid on that, at one time, considering this stock at par, $35,000, and we withheld to straighten these titles out, to the Standard Pocahontas

Coal Company, 600 acres of coal, which we valued anywhere from $50,000 to $150,000; we settled two or three other claims, and I do not think I am quite now qualified to speak about, of, I think I have them in my file there, some two thousand dollars more.

This would indicate a cost to the petitioner corporation of from $407,000 to $507,000. The evidence as to the March 1, 1913, value of the property is vague. In 1915, an engineer representing the Old Dominion Trust Co. of Richmond, Va., made a report on the company's property in which he stated that there were approximately 20,000,000 tons of mineable coal at an average value of five cents per net ton making a total value of $1,000,000. On or about December 31, 1917, an account was entered upon the corporation's general ledger debiting coal lands (47) $1,000,000 with the following explanation:

Estimated value as of March 1, 1913 of 6,000 acres coal land said to contain 20,000 tons of coal at five cents per ton.

The income-tax returns filed for those years claimed a March 1, 1913, value for the property of $1,000,000.

In United States v. Ludey, 274 U. S. 295, it was stated:

* * * The amount of the allowance for depreciation is the sum which should be set aside for the taxable year, in order that, at the end of the useful life of the plant in the business, the aggregate of the sums set aside will (with the salvage value) suffice to provide an amount equal to the original cost. * * *

* * * * * * * * * *

The depletion charge permitted as a deduction from the gross income in determining the taxable income of mines for any year represents the reduction in the mineral contents of the reserves from which the product is taken.

No essential difference is recognized in the decisions of the courts between depreciation and depletion, so far

as the nature of the deduction under the taxing acts involved is concerned. Both are designed to return to the taxpayer the cost or March 1, 1913, value of property depreciated or depleted, whichever is the basis for the computation.

The evidence in the instant proceedings is that there was an estimated quantity of coal in place on March 1, 1913, of 37,608,642 tons. No contention is made anywhere that the March 1, 1913, value of this coal in place was in excess of $1,000,000. The depletion unit used by the respondent in his computation of $0.036 per ton will, (48) upon the exhaustion of the coal deposits, return to the petitioner corporation a total of $1,353,911.11. The depletion rate used by the respondent will therefore return to the petitioner corporation an amount in excess of the greatest claim made by it as to the value of the coal in place at March 1, 1913.

The respondent has determined that a depletion rate of $0.036 per ton is a reasonable rate. The Commissioner's determination of tax liability is prima facie correct. United States v. Rindskopf, 105 U. S. 418; Avery v. Commissioner, 22 Fed. (2d) 6; Brown v. Commissioner, 22 Fed. (2d) 797; Blair v. Roth, 22 Fed. (2d) 932. If the corporation is entitled to a higher rate of depletion than that determined by the respondent the burden is upon the corporation to prove the inadequacy of the depletion rate used by the respondent. We are of the opinion that it has not sustained that burden of proof.

In Docket No. 14517 the Bankers Pocahontas Coal Co. claims that its income for 1920 was overstated by the inclusion therein of royalties in the amount of $5,434.66 and taxes in the amount of $180, which were taxable as income of the year 1919, for which year the amounts were returned as income. The evidence indicates that the books of account show these receipts in 1920. It is contended, however, that the amounts were actually received by the corporation in 1919 and that it was through negligence that the amounts were not deposited in the bank until 1920. The evidence supports such claim. The contentions of the corporation upon this point are there- (49) fore sustained.

In Docket No. 42664 it is contended that a certain receipt of the corporation in 1924, amounting to $3,770.40, from the Flanagan Coal Co., did not constitute a receipt of income. This amount was received in compromise of a suit brought against that company by the petitioner "to recover the value of the coal that had been extracted, plus damages to the plant." At the hearing of these proceedings petitioner's president was asked to relate "the facts briefly out of which the condition arose which resulted in the receipt of that amount of money [$3,770.40] in 1924 by your company." Petitioner's president testified:

The Flanagan Coal Company owned an adjoining piece of land to our land; we discovered that they had mined across our boundary line in a particular seam of coal; I took that up with them and they first said they would pay for it. The matter hung on for some months; this was in 1920 when they had gone in there, at which time the price of coal was very high—anywhere from $6.00 to $15.00 a ton. They did not pay, and when I got my engineers to go down to undertake to measure up how much coal they had gotten out, they found out they had shot in the entries and we could not get in at all, so I brought a suit for damages to the property, and we eventually settled it and we got this $3,770 in 1924, for damage to our property, and that seam of coal I figured and figured over with my engineers as at least $10,000 because they had absolutely destroyed the method of going in on that side of the hill.

He further testified on cross-examination:

We claimed our damages very considerably in excess of that [$3,770.40], but the Flanagan Coal Co. at that time was in a pretty precarious condition financially, and we figured every little bit would help, and we got as (50) much as we could.

The respondent determined that the $3,770.40 in question was a part of the petitioner's gross income; that the trespasser had mined 15,000 tons of coal from the corporation's land; and that the petitioner was entitled to deduct from gross income, in its tax return for 1924, $540 for depletion in respect of the coal removed.

The taxing acts permit the deduction from gross income of losses sustained during the taxable year when not compensated for by insurance or otherwise. (Section 234 (a) (4), Revenue Acts of 1918 and 1921.) If there was a loss sustained by the Bankers Pocahontas Coal Co. as a result of the tortious act of the Flanagan Coal Co., it was sustained in 1920, and the amount of the loss not compensated for by insurance or otherwise is deductible from the gross income of 1920. The evidence does not, however, afford facts from which the amount of the loss may be determined. We do not know what the cost of the coal removed by the trespasser was to the petitioner nor its March 1, 1913, value. If the Banker's Pocahontas Coal Co. is predicting the loss and damage to the property upon the inflated prices of coal in 1920, we think there is no justification for basing a deductible loss upon such inflated values. Joseph E. Hubinger, 13 B. T. A. 960, affirmed by the Circuit Court of Appeals for the Second Circuit December 2, 1929. The deduction of any loss for 1920 must therefore be disallowed for lack of proof of (51) the amount of the loss, if any.

The same situation obtains with respect to the year 1924. The company received from the trespasser $3,770.40. The petitioner has found that all but $540 of this amount (which he has allowed as a deduction from gross income as depletion) constituted taxable income of the company for 1924. The company has submitted no evidence that the cost or March 1, 1913, value of the coal removed by the trespasser was in excess of $540 or that such basis plus damages to the property was in excess of $540. The determination of the Commissioner is therefore sustained for lack of evidence showing error on the part of the respondent. Joseph E. Hubinger, supra.

In Docket No. 14517, with respect to the year 1920, and in Docket No. 14516, with respect to the year 1921, additional error is alleged in the adjustment of surplus and, therefore, in the computation of the petitioner corporation's invested capital. The correctness of the adjustment depends upon the determination of a proper depletion allowance. It therefore follows that, when a proper depletion rate has been determined under the major issue

of the proceedings, the establishment of a proper depletion reserve and, consequently, the proper adjustment of surplus will necessarily follow and be made the subject of appropriate recomputation under the Rule 50 settlement.

With respect to the years 1920 and 1921, the corporation also claims that there has been an improper proration of dividends affecting its invested capital for those years. This raises the question of a tentative tax adjust-
(52) ment such as was involved in L. S. Ayers & Co., 1 B. T. A. 1135. The rule of the Board in L. S. Ayers & Co., supra, should be applied in the recomputation of the deficiencies.

The only issues raised in the three proceedings taken by D. J. F. Strother relate to an overstatement of his income for the years in question resulting from the inclusion therein of the dividends received by him from the corporation. The respondent submits that the determination of the nature of the receipt by the corporation under the leases will also determine the nature of the dividends paid out of its receipt to the stockholder. To the extent that the distribution made by the corporation constitutes a distribution of its depletion reserve the amount received by Strother in nontaxable. Parties are in full accord as to the treatment to be given the individual appeals.

Reviewed by the Board.

Judgment will be entered
under Rule 50.

MOTION FOR REHEARING AND MODIFIED FINDINGS OF FACT AND OPINION

(53) Filed Feb. 27, 1930.

U. S. BOARD OF TAX APPEALS

Bankers Pocahontas Coal Company,
Petitioner,

vs. Docket Nos. 14516-17 and 42664.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

vs. Docket Nos. 10472, 25275 and 32170.

Commissioner of Internal Revenue,
Respondent.

Come the petitioners herein, and move the Board to set aside its findings of fact and decision promulgated in the above entitled appeals on January 22, 1930, (providing for a Rule 50 redetermination) and to grant petitioners a rehearing, or modified findings of fact and opinion herein, for cause:

1. That the Board erred in including in said findings of fact, statements concerning the contracts upon the property, the estimated recoveries of coal tonnage on March 1, 1913, and the tonnage mined and royalty receipts from each of the several leases; which said evidence was offered at the hearing (record p. 124) by stipulation of parties only for purposes of any computation under Rule 50, and which said evidence was not introduced nor available as the basis of any findings of fact in reference to the issues between the parties herein.

2. Petitioners move to strike from said findings of fact, the sentence "the cose to the corporation of the

properties acquired by it was between $407,000 and $507,-000", because said evidence was irrelevant and incompetent, and was received over the objections of petitioners.

3. That the Board erred in its conclusion of law that the agreements herein between the corporate petitioner and operating companies should not be held to be sales of coal in place, being the legal construction admitted to attach to said agreements under the laws of West Virginia.

4. That the Board erred in setting forth evidence in its opinion, concerning the value of the property on March 1, 1913, which evidence is not set forth in its findings of fact.

5. That the Board erred in not including in its find-
(54) ings of fact, that amount of the depletion allowable to the corporate petitioner is res adjudicata herein under the decision of Bankers Pocahontas Coal Co. vs. Albert White, Collector, and, also, under its findings of fact that the subject matter of said decision and the parties therein are identical with those involved in the present proceedings.

6. That the Board erred in stating in its opinion additional evidence as to the cost of the properties was introduced and also regarding the estimated tonnages in each of the leases; it appearing said evidence was taken over the objections of petitioners upon cross examination by respondent, and otherwise was introduced subject to stipulation only for purposes of a Rule 50 computation.

7. That the Board erred in holding the damages recovered from the Flanagan Coal Company constitute a recovery of the value of coal mined, subject to allowance for depletion, as contradictory to its findings of fact thereon.

8. That the Board having erred as aforesaid, in its decision of the Bankers Pocahontas Coal Company appeal likewise erred in applying its principles to decision of the appeals of petitioner Strother.

And, it appearing this decision was reviewed by the Board, Petitioners request that this motion for rehearing and modification be reheard by the Board.

(s) CAMDEN R. McATEE,
Attorney for Petitioners.

(55) **ORDER**

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Co.,
Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 14516, 14517, 42664, 10472, 25275, 32170.

Counsel for petitioners in the above entitled proceedings having filed a motion with the Board on February 27, 1930, for a rehearing or for modified findings of fact and opinion as set forth in the report promulgated January 22, 1930, alleging that the Board erred in including in said findings of fact certain data contained in a stipulation which counsel now claims was introduced solely for purposes of any recomputation under Rule 50; that a certain finding of fact be stricken from the report on the ground that the evidence supporting said finding of fact was irrelevant, incompetent, and received over objection of counsel for petitioners; that the Board erred in several conclusions of law as set forth in its opinion and in not including in its findings of fact a certain other conclusion of law to the effect that the amount of allowable depletion is res adjudicata; that the Board

erred in setting forth certain evidence in its opinion, and the premises considered and due consideration having been given thereto as well as to statements of counsel for the petitioners at the hearing in the above entitled proceedings and to his then position with respect to the matters presently complained of, and after reconsideration of the record herein, it is

ORDERED that the motion be and the same is hereby denied.

(Signed) CHARLES P. SMITH
Member,
United States Board of Tax Appeals.

Washington, D. C.

Entered: March 6, 1930.

CPS:aa.

NOTICE OF SETTLEMENT

(56) Filed Mar. 31, 1930.

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

v. Docket Nos. 10472-25275-32170

Commissioner of Internal Revenue, Respondent.

The annexed proposed determination of deficiency under the opinion of the Board of Tax Appeals heretofore rendered herein will be presented to the Board for settlement on the .... day of ..... 1929, at 9.30 A. M.

This notice of proposed determination is submitted in accordance with the decision of the Board without prejudice to the Commissioner's right to contest the correct-

ness of the decision pursuant to the statute in such cases made and provided.

(Signed) C. M. CHAREST
C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

OF COUNSEL:

MAXWELL E. McDOWELL,
FRANK B. SCHLOSSER,
Special Attorneys,
Bureau of Internal Revenue.

(57) STATEMENT

IT:AR:F-6
LGS

In re: D. J. F. Strother,
Welch, West Virginia.

Docket Nos. 10472-25275-32170.

Years	Additional Tax	Over Assessment
1919	$ 404.83	
1920	145.87	
1921	536.04	
1922	2,188.61	
1923	1,670.74	
1924		$ 36.38
1925	860.02	
Totals	$5,806.11	$ 36.38

Net additional tax $5,769.73

1919

Net income, 60-day letter			$23,203.28
Deduct:			
Dividends received from Bankers Pocahontas Coal Co., 60-day letter		$11,372.50	
Correct amount taxable Board's decision		4,762.69	6,609.81
Net income adjusted			$16,593.47
Less:			
Exemption	$2,000.00		
Dividends	6,485.69		
Interest United States obligations	189.98		8,675.67
Income subject to normal tax			$7,917.80
4% on $4,000.00		$160.00	
8% on $3,917.80		313.42	$ 473.42
Surtax on $16,593.47			$ 451.54
Tax liability			$ 924.96
Previously assessed			520.13
Additional tax			$ 404.83

(58) 1920

Net income, 60-day letter			$30,728.86
Deduct:			
Dividends received from Bankers Pocahontas Coal Co., 60-day letter		$16,110.00	
Correct amount taxable Board's decision		7,235.48	8,874.52
Net income adjusted			$21,854.34

Less:			
Exemption	$2,000.00		
Dividends	9,291.48		
Interest United States obligations	332.50		11,623.98
Income subject to normal tax			$10,230.36
4% on $4,000.00		$160.00	
8% on $6,230.36		498.43	$ 658.43
Surtax on $21,854.34			876.89
Tax liability			$1,535.32
Previously assessed			1,389.45
Additional tax			$ $145.87

1921

Net income, 60-day letter			$27,031.14
Deduct:			
Dividends received from Bankers Pocahontas Coal Co.,			
60-day letter		$16,112.50	
Board's decision		10,595.74	5,516.76
Net income adjusted			$21,514.38
Less:			
Exemption	$2,000.00		
Dividends	13,403.74		15,403.74
Income subject to normal tax			$ 6,110.64
4% on $4,000.00		$160.00	
8% on $2,110.64		168.85	$ 328.85
Surtax on $21,514.38			846.30
Tax liability			$ 1,175.15
Previously assessed			639.11
Additional tax			$ 536.04

(59)

	1922		
Net income, 60-day letter			$44,421.09
Deduct:			
Dividends received from Bankers Pocahontas Coal Co.,			
60-day letter		$16,128.00	
Board's decision		14,253.12	1,874.88
Net income adjusted			$42,546.21
Less:			
Exemption	$2,000.00		
Dividends	16,297.12		18,297.12
Income subject to normal tax			$24,249.09
4% on $4,000.00		$160.00	
8% on $20,249.09		1,619.93	$ 1,779.93
Surtax on $42,546.21			3,423.78
Tax liability			$ 5,203.71
Previously assessed			3,015.10
Additional tax			$ 2,188.61
	1923		
Net income, 60-day letter			$46,675.00
Deduct:			
Dividends received from Bankers Pocahontas Coal Co.,			
60-day letter		$13,888.00	
Board's decision		12,941.53	946.47
Net income adjusted			$45,728.53
Less:			
Exemption	$2,000.00		
Dividends	16,465.53		18,465.53
Income subject to normal tax			$27,263.00

4% on $4,000.00		$ 160.00	
8% on $23,263.00		1,861.04	$ 2,021.04
Surtax on $45,728.53			4,045.71
Total			$ 6,066.75
Less:			
Credit of 25%—Sec. 1200, Revenue Act of 1924			1,516.69
Tax liabilty			$ 4,550.06
(60)			
Previously assessed		$3,839.09	
Less:			
Credit of 25%, Sec. 1200, Revenue Act of 1924		959.77	2,879.32
Additional tax			$1,670.74

1924

Net income, 60-day letter			$26,910.76
Deduct:			
Dividends received from Bankers Pocahontas Coal Co.,			
60-day letter		$16,400.00	
Board's decision		14,651.92	1,748.08
Net income adjusted			$25,162.68
Less:			
Exemption	$2,500.00		
Dividends	17,611.92		20,111.92
Income subject to normal tax			$ 5,050.76

2% on $4,000.00	$80.00	
4% on $1,050.76	42.03	$ 122.03
Surtax on $25,162.68		521.39
Total		$ 643.42
Earned income credit		55.00
Tax liability		$ 588.42
Previously assessed		624.80
Overassessment		$ 36.38

1925

Net income, 60-day letter			$42,358.02
Deduct:			
Dividends received from Bankers Pocahontas Coal Co.,			
60-day letter		$11,920.00	
Board's decision		9,311.31	2,608.69
(61) Net income adjusted			$39,749.33
Less:			
Exemption	$3,500.00		
Dividends	14,429.31		17,929.31
Income subject to normal tax			$21,820.02
1½% on $4,000.00		$ 60.00	
3% on $4,000.00		120.00	
5% on $13,820.02		691.00	$ 871.00
Surtax on $39,749.33			1,774.93
Total			$2,645.93
Earned income credit			206.25
Tax liability			$2,439.68
Previously assessed			1,579.66
Additional tax			$ 860.02

(62) STATEMENT OF ACCOUNT

IT:AR:F-6
LGS

In re: D. J. F. Strother,
Welch, West Virginia.

Docket Nos. 10472-25275-32170.

1924

Original tax assessed #90241	$624.80
Tax paid	$624.80
Tax liability	588.42
Overpayment	$ 36.38

(63) **ORDER**

UNITED STATES BOARD OF TAX APPEALS

Washington

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 10472, 25275, 32170.

Pursuant to the Board's findings of fact and opinion promulgated in the above entitled proceedings January 22, 1930, counsel for the respondent filed a notice of settlement on March 31, 1930. At the hearing under Rule 50, on June 18, 1930, counsel for the petitioner moved that the entry of judgment in these proceedings be continued until the Board should have disposed of certain contentions made by counsel for the petitioner with respect to the proceedings involving Bankers Pocahontas Coal Co., Docket Nos. 14516, 14517, and

42664. Counsel for the respondent interposed no objections to the granting of the motion. Wherefore, it is—

ORDERED that the hearing under Rule 50 involving Docket Nos. 10472, 25275, and 32170 be continued and placed on the Day Calendar for hearing on August 13, 1930.

(Signed) CHARLES P. SMITH,
Member,
United States Board of Tax Appeals.

Entered: July 15, 1930.

CPS:aa.

OBJECTIONS AND COUNTER PROPOSAL AS RULE 50 SETTLEMENT OFFERED BY PETITIONER

(64) Filed Aug. 12, 1930

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

vs. Docket Nos. 10472, 25275, 32170

Commissioner of Internal Revenue, Respondent.

Respondent having filed its Rule 50 proposal for tax determination herein based upon Board opinion and proposal in Nos. 14516, 14517 and 42664, Bankers Pocahontas Coal Company vs. Commissioner, and consideration thereof being continued by Board order of July 15, 1930 to August 13, 1930 and until after contentions in said Bankers case were to be disposed of by the Board,

Comes petitioner by his attorney, and objects to the proposed settlement herein and offers a proposed counter determination for cause as follows:

1. Petitioner is a stockholder in said Bankers Poca-

hontas Coal Company, which is upon a cash receipt basis and distributing its entire income in the several (65) years, and derives material income therefrom as dividends.

2. The Board has determined allowable depletion in the several years to said Bankers company is computed upon tonnage mined and not upon tonnage paid for; that said unit is .036 per ton, and not .05 per ton as determined by alleged res adjudicata proceedings, and that payments to said Bankers company under the operating contracts are royalties subject to depletion allowances, and not proceeds of sale of coal, and thereby has denied contentions of said Bankers company, which are material to determination of the tax liability of petitioner, and petitioner expressly reserves the right hereafter to contest said several rulings in the Bankers case as affecting his own tax liability in each and all years to which same are applicable.

3. Petitioner states the depletion allowances made to the Bankers Company are each erroneous as to amount and determination on tonnage mined, and said errors are reflected in use of same in computing his tax liability in the proposal of respondent.

4. Petitioner states the Bankers opinion states distributed depletion reserve is non taxable to Strother (66) but same is not shown in respondent's computation.

5. That in said computation Bankers dividends to petitioner are shown in varying amounts for each year from 1919 to 1925 inclusive and the exclusion of a less amount of dividends than received for the years 1919, 1920 and 1921 is shown in the computation of net income subject to normal tax, and petitioner has no certainty of the computation for succeeding years.

6. That so-called correct amounts of said dividends taxable under the Bankers decision to petitioner are shown for the several years but no method of deriving same or establishing the items is given, and petitioner objects to the statement or computation of net income

thereby obtained as insufficient to establish a tax liability herein.

7. The stockholding of petitioner being 454.50 shares of 1500 shares outstanding or 30.3% and respondent not having eliminated receipt of depreciation reserve distributed, petitioner amends the computation of respondent as to dividends excluded for normal taxes and said reserve and restates the tax liability thereby as follows:

(67) 1919

Adjusted net income			$16,593.47
Less 30.3% of $..... depletion			$.....
Corrected net income			$.....
Less exemption	$ 2,000.00		
	11,372.50		
Dividends	$.....		
U. S. Int.		189.98	$.....
Income subject to normal tax			$.....
4% on $4,000		$.....	
8% on $.....		$.....	
Surtax on $.....		$.....	$.....
Tax liability			$.....
Previously assessed			$.....
Additional Tax			$.....

Insertion of depletion allowed necessary to complete figures.

1920

Adjusted net income			$21,854.34
Less 30.3% of $16,423.02			4,931.83
Corrected net income			$17,922.51
Less Exemption		$2,000.00	
Dividends	$16,110.00 4,931.83	11,178.17	
U. S. Int.		332.50	13,510.67
Income subject to normal tax			$ 4,411.84
4% on $4,000.00		160.00	
8% on 411.84		32.85	192.85
Surtax $17,922.51		$410.00 134.58	544.58
Tax Liability			$ 737.43
Assessed			1,389.45
Overassessment			$ 652.02

(68) 1921

Adjusted Net Income			$21,514.38
Less 30.3% of $11,921.87			3,618.27
Corrected net income			$17,896.11
Less Exemption		$2,000.00	
Dividends	$16,110.00 3,618.27	12,491.73	14,291.73
Subject to normal tax			$ 3,604.38
4% on	$3,604.38	$144.18	
Surtax on	$17,896.11	542.73	
Total tax			$ 686.91
Assessed			639.11
Additional			$ 47.80

1922

Adjusted net income			$42,546.21
Less 30.3% of $16,799.36			5,090.21
Corrected net income			$37,456.00
Less Exemption		$ 2,000.00	
	$16,297.12		
	5,090.21	11,206.91	13,206.91
Income subject to normal tax			$24,249.09
4% on $4,000		$ 160.00	
8% on $20,249.09		1,619.39	$1,779.39
Surtax on $37,456.00			2,532.96
Tax liability			$ 4,312.35
Assessed			3,015.61
Additional			$1,296.74

(69) 1923

Net Income adjusted			$45,728.53
Less 30.3% of $17,177.79			5,204.87
Corrected net income			$40,523.66
Less exemption		$2,000.00	
	16,465.53		
Dividends	5,204.87	11,260.66	13,260.66
Income subject to normal tax			$27,263.00
4% on $4,000.00		$ 160.00	
8% on $23,263		1,861.04	$2,021.04
Surtax on $40,523.66			3,054.26
			$5,075.30
Less 25% cr.			1,268.82
			$3,806.48
Assessed	$3,839.09		
25%	959.77		2,879.32
Additional			$ 927.16

1924

Adjusted Net income			$25,162.68
Less 30.3% of $20,553.41			6,227.68
Corrected net income			$18,935.00
Less Exemption		$2,000.00	
	$17,611.92		
	6,227.68	11,383.24	13,383.24
Income subject to normal tax			$ 4,551.76
2% on $4,000	$80.00		
4% on $551.76	22.07	$102.07	
Surtax on $18,935.00		177.40	
		$279.47	
Earned Income credit		55.00	
Tax liability		$224.47	
Assessed		624.80	
Overassessment		$400.33	

(70) 1925

Adjusted Net Income			$39,749.33
Less 30.3% of $18,851.47			5,712.10
Corrected net income			$34,037.23
Less exemption		$3,500.00	
	$14,429.31		
Dividends	5,712.10	8,717.21	12,217.21
Subject to normal tax			$21,820.02
1½% on $4,000	$ 60.00		
3% on $4,000	120.00		
5% on $13,820.02	691.00		871.00
Surtax on $34,037.23			1,324.10
Total tax liability			$2,195.10
Assessed			1,579.66
Additional			$ 615.44

Summary

Year	Respondent		Petitioner		
1919	Add $ 404.83		Not figured		
1920	Add 145.87		Over		$ 652.02
1921	Add 536.04		Add	$ 47.80	
1922	2,188.61		Add	1296.74	
1923	1,670.74		Add	927.16	
1924	Over	$36.38	Over		400.33
1925	860.02		Add	615.44	
	$5,806.11			$2,897.14	
	36.38			1,052.33	
Net add	$5,769.73			$1,844.81	$1,052.33

(71) In petitioner's computation the adjustment for depletion reserve follows the Bankers decision that same is computed on coal mined. This leads to error as dividends were further received based on coal paid for and such payment includes a depletable or depreciable capital return of the value of the contract or commodity, which capital receipt by petitioner cannot be eliminated in the computation of his net income under the Board method.

Petitioner submits the foregoing tentative computation without prejudice to and reserving his right to further contest same as provided by law.

(s) CAMDEN R. McATEE,
Attorney for Petitioner.

PETITIONER'S AMENDED COUNTER RULE 50 PROPOSAL

(72) Filed Sept. 2, 1930.

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

vs. Docket Nos. 10472
25275
32170

Commissioner of Internal Revenue,
Respondent.

For amended objections and counter Rule 50 proposal, petitioner D. J. F. Strother respectfully shows the Board as to the proposed determination for the several years.

(a) The findings of fact are that the Bankers Pocahontas Coal Company in the several years received amounts from its operating contracts and entirely distributed them including any depletion reserve to its stockholders including this petitioner, and that respondent made this petitioner no allowance for any depletion reserve. The opinion is that to the extent the distributions of the corporation are non-taxable the amounts received by this petitioner are non-taxable.

(b) In the several years this petitioner held 30.3%
(73) of the capital stock of petitioner and is thereby entitled to a non-taxable allowance as follows:

	Total Depletion	Allowable Strother	Allowed Strother
1919	$--------	$-------	$6,609.81
1920	16,423.02	4,931.83	8,874.52
1921	11,921.87	3,618.27	5,516.76
1922	16,799.36	5,090.21	1,874.88
1923	17,177.79	5,204.87	946.47
1924	20,553.41	6,227.68	1,748.08
1925	18.851.47	5,712.10	2,608.69

Adjusting the proposed determination of respondent to all depletion reserves and thereby correct dividend adjustments for normal taxes, we have the following computation:

1919—Not computed as special depletion not available.

1920

Net Income			$30,728.86
Bankers dividends		$16,110.00	
Depletion reserve adjustment		11,781.17	4,931.83
For surtax Taxable net income			$25,797.83
Less:	$ 2,000.00		
	13,837.17		
	332.50		16,169.67
For normal tax			$ 9,626.16
(74) 4% on $4,000			$ 160.00
8% on $5,626.16			450.09
Surtax $25,797.83			1,387.76
Tax liability			$1,997.85
Assessed			1,389.45
Add			$ 608.40

1921

Net Income			$27,031.14
Bankers Dividends		$16,112.50	
Depletion reserve adjustment		12,494.23	3,618.27
For surtax Taxable net income,			$23,412.87
Less:		$ 2,000.00	
		15,302.23	17,302.23
For normal tax			$ 5,110.64

4% on $4,000		$ 160.00
8% on $1,110.64		88.85
Surtax on $23,412.87		1,031.28
Tax liability		$1,280.13
Assessed		639.11
Add.		$ 641.02

(75) 1922

Net Income		$44,421.09
Bankers Dividends	$16,128.00	
Depletion reserve adjustment	11,027.79	5,090.21
For surtax Taxable net income		$39,330.88
Less:	$ 2,000.00	
	14,651.79	16,651.79
For normal tax		$22,679.09
4% on $4,000		$ 160.00
8% on $18,679.09		1,494.32
Surtax $39,330.88		2,856.24
Total		$4,510.56
Assessed		3,015.10
Add.		$ 1,395.46

1923

Net income		$46,675.00
Bankers Dividends	$13,888.00	
Depletion reserve adjustment	8,683.13	5,204.87
For surtax Taxable net income		$41,470.13

Less:	$ 2,000.00	
	12,207.13	14,207.13
For normal tax		$27,263.00
4% on $4,000		$ 160.00
8% on $27,263.00		2,181.04
Surtax $41,470.13		3,224.62
Total		$ 5,565.66
Less 25 cr.		1,391.41
Liability		$ 4,174.25
Assessed	$ 3,839.09	
Less 25%	959.77	2,879.32
Additional		$ 1,294.93

(76) 1924

Net income		$26,910.76
Bankers Dividends	$16,400.00	
Depletion reserve adjustment	10,172.32	6,227.68
For surtax Taxable net income		$20,683.08
Less:	$ 2,500.00	
	13,132.32	15,632.32
For normal tax		$ 5,050.76
2% on $4,000		$ 80.00
4% on $1,050.76		42.03
Surtax $20,683.08		254.15
		$376.18
Earned Income Credit		55.00

Liability		$ 321.18
Assessed		624.80
Over.		$ 303.62

1925

Net Income		$42,358.02
Bankers Dividends, Depletion reserve adjustment		5,712.10
For surtax, Taxable net income		$36,645.92
Less:	$ 3,500.00	
	21,325.90	24,825.90
For normal tax		$11,820.02
1½% on $4,000	$ 60.00	
3% on $4,000	120.00	
5% on $3,820.02	191.00	
		$ 371.00
Surtax on $36,645.92		1,617.50
		$ 1,988.50
Credit		206.25
Liability		$ 1,782.25
Assessed		1,579.66
Add.		$ 202.59

(77) Summary:

1920	$ 608.40	
1921	641.02	
1922	1,395.46	
1923	1,294.93	
1924		$ 303.62
1925	202.59	
	$ 4,142.40	
	303.62	
	$ 3,838.78	

Petitioner submits the foregoing amended tentative computation without prejudice to and reserving his right to further contest same as provided by law.

(s) CAMDEN R. McATEE,
Attorney for Petitioner.

SUPPLEMENT TO PETITIONER'S AMENDED COUNTER RULE 50 PROPOSAL

(78) Filed Sept. 10, 1930.

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

vs. Docket Nos. 10472, 25275, 32170

Commissioner of Internal Revenue, Respondent.

Petitioner herewith supplies his 1919 tax computation, omitted from the original amended counter proposal as follows:

1919

Net Income		$23,203.28
Bankers Dividends	$11,372.50	
Depletion Reserve Adjustment	3,592.25	7,780.25
For Surtax Taxable Net Income		$15,423.03
Less	$2,000.00	
	5,315.25	
	189.98	7,505.23
For Normal Tax (same as respondent)		$ 7,917.80
Normal Tax		473.42
Surtax on $15,423.03		375.38
		$ 848.80
Previously assessed		520.13
Additional		$ 328.67

CAMDEN R. McATEE,
Attorney for Petitioner.

(79) **ORDER**

UNITED STATES BOARD OF TAX APPEALS

Bankers Pocahontas Coal Co.,
Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 10472, 14516, 14517, 25275, 32170, 42664.

It appearing as a result of a hearing on the notice of settlement of the deficiencies of D. J. F. Strother, Docket Nos. 10472, 25275, and 32170, that there is an error in the last paragraph of the findings of fact of the Board, promulgated January 22, 1930, 18 B. T. A. 901, it is

ORDERED that the last paragraph of said findings of fact be deleted and that there be substituted therefor the following paragraph:

In the several years involved herein the petitioner, Strother, as one of the corporation's stockholders, received payments from the Bankers Pocahontas Coal Co. and reported same in his returns but did not return them as taxable income. The corporation received the royalties of the contracts, used such portion as was necessary for payment of the ordinary and necessary expenses of administering business, set aside a certain reserve to meet pending Federal taxes and distributed the rest to the stockholders. No allowance was made by the Commissioner to the petitioner, Strother, for any depletion reserve received by him and the Commissioner added the entire receipts to his net income and has determined deficiencies accordingly.

(Signed) CHARLES P. SMITH,
Member, United States
Board of Tax Appeals.

Washington, D. C.,

Entered September 26, 1930.

(80) **DECISION**

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

v.

Commissioner of Internal Revenue,
Respondent.

Docket Nos. 10472, 25275, 32170.

Pursuant to the findings of fact and opinion of the Board, promulgated in the above entitled proceeding under date of January 22, 1930, the respondent, on March 31, 1930, filed a notice of settlement in which deficiencies were recomputed for the years 1919 to 1925, inclusive. On September 2, 1930, the petitioner filed an alternative notice of settlement showing deficiencies differently from those determined by the respondent. After hearing thereon on September 3, 1930, and after considering arguments of counsel, the redeterminations of the respondent are found to be in accordance with the findings of fact and opinion promulgated by the Board on January 22, 1930. Wherefore, it is

ORDERED and DECIDED that there are deficiencies in income tax for the years 1919, 1920, 1921, 1922, 1923, and 1925 of $404.83, $145.87, $536.04, $2,188.61, $1,670.74, and $860.02, respectively, and that there is an overassessment for 1924 to be abated in the amount of $36.38.

(Signed) CHARLES P. SMITH,
Member, United States
Board of Tax Appeals.

Washington, D. C.,

Entered Sep. 29, 1930.

PETITION FOR REVIEW

(81) Filed Jan. 6, 1931.

CIRCUIT COURT OF APPEALS OF THE UNITED STATES
FOURTH CIRCUIT

D. J. F. Strother, Appellant,

vs. Docket No.-----

Commissioner of Internal Revenue,
Appellee.

Petitioner appellant, D. J. F. Strother, being aggrieved by a deicsion of the United States Board of Tax Appeals, (hereinafter called "the Board"), determining additional income taxes of $5,706.11 and legal interest for the calendar years 1919 to 1925, inclusive, as entered on September 29, 1930, in the appeal of D. J. F. Strother vs. Commissioner of Internal Revenue, Nos. 10472, 25275 and 32170 (consolidated) on the docket of said Board, hereby respectfully submits his petition for review thereof by this Court, and for cause in support thereof, states (82) as follows:

1. Now and at the times hereinafter mentioned, petitioner appellant was and is a citizen of the United States and resident of the State of West Virginia, within the jurisdiction of this Court, and prosecutes this proceeding in his own right, pursuant to Sections 1001-2 of the Revenue Act of 1926. Appellee is the duly appointed and qualified Commissioner of Internal Revenue, and is joined herein as a party in his official capacity.

2. For the calendar years 1919 to 1925, inclusive, this appellant made and filed his income tax returns to disclose the gross income and the deductions of credit against same allowed by the several Revenue Acts as computed upon a cash receipts and disbursements basis, and to permit assessments of tax upon the resulting income, if any, and paid any tax shown thereby for each of the said taxable years.

3. In each of said taxable years the major portion of the gross income of appellant, and which is here in controversy, consisted of the dividends received from the Bankers Pocahontas Coal Company, (hereinafter called the "Bankers Company"), a corporation owning certain West Virginia coal lands and certain contracts thereon, (83) whereby operating companies paid money payments each year to said Bankers Company for the mining and taking by them of coal from said lands; and which contracts were executed and existing before and continuous since March 1, 1913, during which time appellant has been a stockholder and officer of said Bankers Company. As appellant is advised, said Bankers Company likewise made its income tax returns for the

several years aforesaid, and therein did not report said money receipts as any part of the taxable net income, for cause, that said Bankers Company claimed and alleged the money payments were the proceeds of sales of coal in place affected and determined by said contracts before March 1, 1913 and thereafter continued, and thereby not subject to income tax. In his several returns, this appellant likewise disclosed the receipt of said dividends received by him each year from the Bankers Company, but did not report same as income subject to tax, for cause that, appellant likewise claimed said payments were not taxable income.

4. Upon review and examination of said returns of appellant, the appellee, Commissioner of Internal Revenue, having ruled the money payments to the Bankers Company in the several years constituted payments of royalties by lessees to a lessor, and were taxable to the (84) Bankers Company in the several years received to the extent that said receipts exceeded any return of capital therein received, further ruled the dividends paid to this appellant by the Bankers Company were taxable, and did not exclude therefrom as non-taxable any depletion reserve distribution received by this appellant in said dividends. The taxable net income reported by this appellant in his several returns was accordingly adjusted and increased, and the resulting deficiencies in tax were proposed against appellant by official letters from the appellee Commissioner.

5. Whereupon, within the time and as allowed by law, this appellant, alleging error of law and fact therein, on the part of appellee Commissioner, appealed to said Board from said official findings as to each of said adjustments and the resulting tax proposals, praying a redetermination thereof, and issue was joined on said appeals by answer filed by the appellee Commissioner.

6. At the hearing of said appeals by the Board on May 3, 1929, by agreement, same were consolidated and heard with appeals of the Bankers Company, a corporation, in which this appellant was and is an officer and stockholder and from which the sums in controversy (85) were received by appellant as dividends. It ap-

peared in said hearing the determination of the issues of said appeals of Bankers Company would substantially decide the issues made in the appeals of this appellant, and the evidence and proceedings in said Bankers appeals were by consent of parties considered as read into the appeals of this appellant.

The evidence so read related to the issues in the Bankers Company appeals as to whether its money payments under certain contracts constituted non taxable income as the proceeds of sales of coal in place accomplished before March 1, 1913, or were royalties payable by lessees to their lessor, and the proper rate of depletion allowable to the lessor in the latter event.

In addition thereto, this appellant testified as an officer of the Bankers Pocahontas Coal Company all such money receipts were distributed each year after deduction of nominal administration expenses, and including any depletion reserve, excepting that an amount was being withheld sufficient for payment of the proposed tax deficiencies asserted and in controversy, and which amount will be distributed to the stockholders if no lia-
(86) bility therefor is established. Appellant further testified individually the Bankers dividends received by him were disclosed but not reported as taxable income in his returns for the several years, and that appellee Commissioner had included same in his taxable net income without any allowance for depletion reserves therein included, and which constitute non-taxable income to appellant not to be so included.

7. Thereafter the findings of fact and decision of the Board promulgated on January 22, 1930 approved the determination of appellee Commissioner that the aforesaid money payments to the Bankers Company were royalties of a lessor subject to allowance for depletion of the property from which derived and that the rate of 3.6 cents per ton of coal mined was a reasonable depletion deduction in the several years, and as to this appellant made the following finding of fact:

"In the several years involved herein the petitioner, Strother, as one of the corporation's stockholders, re-

ceived payments from the Bankers Pocahontas Coal Co. and reported same in his returns but did not return them as taxable income. The corporation received said amounts from its operating contracts and entirely distributed them, including any depletion reserve. No allowance was made by the Commissioner to the petitioner, Strother, for any depletion reserve received by him and (87) the Commissioner added the entire receipts to his net income and has determined deficiencies accordingly."

8. A proposed determination of tax of appellant pursuant thereto being offered by appellee Commissioner, this appellant filed his objections and original and amended counter-proposal, and the parties were heard. It appeared the proposal of appellee Commissioner ascertained the average daily net income of the Bankers Company for each year exclusive of depletion allowances and by comparison of the average net income earned on dividend dates assumed to ascertain the parts of dividends accordingly allocable to earnings and to capital, and thereby the receipts of earnings and capital by this appellant in his individual dividend receipts, whereby the total capital distributions of the Bankers Company did not accord with the deductible depletion, and on the contrary were about $30,000 less than same for all the years in controversy, and which difference appellee Commissioner assumed to explain as equivalent to any amounts retained against the proposed tax liability of the Bankers Company in controversy. It appeared the counter-proposal of this appellant reduced his individual (88) dividend for each year to exclude therefrom the proportion of the annual depletion deduction of the Bankers Company therein included as found to be fact by the Board when entire distribution of the contract money payments was made each year. After hearing the parties, the Board, of its own motion ordered deletion of its finding as to this appellant as above quoted, and substitution therefor of the following:

"In the several years involved herein the petitioner, Strother, as one of the corporation's stockholders, received payments from the Bankers Pocahontas Coal Co. and reported same in his returns but did not return them

as taxable income. The corporation received the royalties of the contracts, used such portion as was necessary for payment of the ordinary and necessary expenses of administering business, set aside a certain reserve to meet pending Federal taxes and distributed the rest to the stockholders. No allowance was made by the Commissioner to the petitioner, Strother, for any depletion reserve received by him and the Commissionr added the entire receipts to his net income and has determined deficiencies accordingly."

Thereupon, on September 29, 1930, the Board approved and ordered the determination of deficiencies proposed by appellee Commissioner to be entered in the following (89) amounts:

1919	$ 404.83
1920	145.87
1921	536.04
1922	2,188.61
1923	1,670.74
1925	860.02

9. Being advised its petition for review is being presented to this Court by the Bankers Company, alleging errors of said Board in its determination of deficiencies, and because said errors, if any, affect the determination of deficiencies against this appellant, appellant respectfully states it is proper said petitions should be consolidated, and this Court should hear and decide the petition for review of the Bankers Company and thereafter here decide the petition for review of this appellant, who hereby consents the decision of said Bankers petition shall control and be decisive as to his alleged rights, excepting the individual issue of determination of his deficiencies, if any.

10. Appellant believes and avers that errors of law and fact were committed by the Board in its aforesaid findings of fact, decision and determinations to the damage and prejudice of appellant as shown by the follow- (90) ing:

ASSIGNMENT OF ERRORS

1-8. Each of the errors, 1-8 inclusive, assigned in its petition for review by the Bankers Company.

9. In not ruling that the amounts set aside to meet any liability for tax deficiencies herein and to be distributed if such liability does not exist were distributed for purposes of determining the amount of depletion reserves received by this appellant as tax exempt income.

10. In approving and entering the tax determination proposed by appellee Commissioner, and failing to approve and enter the amended tax determination proposed by this appellant.

11. In other respects apparent of record.

WHEREFORE, your petitioner appellant prays that the aforesaid decision and determination of said Board entered as aforesaid be reviewed and reversed by this Honorable Court, and for all other and further relief as the Court shall deem meet and proper in the premises.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Appellant.

District of Columbia:

CAMDEN R. McATEE, being duly sworn, deposes (91) and says that he is one of the attorneys for the petitioner appellant; that he knows the contents of the foregoing petition; that to the best of his knowledge and belief the statements therein are true, and that the assignments of error are well taken, and intended to be argued.

CAMDEN R. McATEE,

Subscribed and sworn to before me this 6th day of January, 1931.

ETHEL R. GUISE,
(SEAL) Notary Public.

NOTICE AND SERVICE OF PETITION FOR REVIEW

The General Counsel (Hon. C. M. Charest), Bureau of Internal Revenue, Washington, D. C., will please hereby take notice—

That on January 6th, 1931, a petition for review by the Circuit Court of Appeals of the United States for the Fourth Circuit of the Board decision and determination in the above entitled appeals was filed with the Clerk of said United States Board of Tax Appeals, and a true copy of said petition is herewith served upon you.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioner.

Service of above notice and receipt of copy of petition for review is hereby acknowledged this 6th day of January, 1931.

C. M. CHAREST,
Attorney for Appellee.

STATEMENT OF EVIDENCE

(92) Filed July 14, 1931.

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

vs.

Docket Nos. 10472, 25275, 32170

Commissioner of Internal Revenue, Respondent.

At hearings of the above entitled appeals (consolidated for hearing) on May 3, 1929, and at subsequent adjournments thereof, before Hon. C. P. Smith, Board Member, the following proceedings were had and evi-

dence offered material to the issues presented by petitioner as appellant in his petition for review of said appeals by the United States Circuit Court of Appeals for the Fourth Circuit.

To maintain the issues joined between the parties:

It was stipulated the decision of these appeals should abide and follow decision of Bankers Pocahontas Coal Company vs. Commissioner of Internal Revenue, Docket Nos. 42664, 14516-17, (consolidated for hearing with these (93) appeals), as to the issues of sale of coal in place and amount of depletion unit allowable, this petitioner being a stockholder of said corporation.

To maintain the issues on his part joined, petitioner testified in his own behalf and made offer of various written exhibits and respondent offered no testimony:

The substance of the testimony given, of the exhibits offered and of the proceedings herein, was and is as follows:

D. J. F. Strother, called for petitioner, testified as follows:

I am the individual petitioner of the several appeals filed in my own name. I am also the president and stockholder of the Bankers Pocahontas Coal Company to the extent of about 30%, and was such stockholder during the years 1920 to 1926. During those years I received payments from the Bankers Company as a stockholder in the amounts shown in the several petitions, and made disclosure of same in my several returns. I did not return these amounts as taxable income, and claimed that they were not taxable. The respondent has assumed to declare the entire amount tax-(94) able income, and to assert a deficiency for the several years based upon the entire amount received. No allowance was made against any receipts to correspond with the depletion allowance to the company. The Bankers Company received its income from its several operating contracts. The respondent has held such re-

ceipts as royalties included a depletion reserve. The Bankers Company distributed all of the receipts except we kept a reserve to meet this question of taxation. If no taxes are due and payable to the Government on that question, that reserve will be distributed. The distribution to the several stockholders included the amount allowable to the Bankers Company as a depletion adjustment. The deficiency calculation by the respondent did not make any allowance of the depletion reserve as non-taxable income. The amount of such depletion is in controversy between the Department and the Bankers Company in these proceedings. My claim herein is that I am entitled to have the depletion allowable to the company and received by me eliminated from my income. I do not think the amounts received by me are taxable under the Sixteenth Amendment, but if they are taxable, I am entitled to a depletion rate for what I receive. My believe that they are not taxable is based upon the proposition that contracts make for a sale of coal in place, and that any gains or profits made were made before March 1, 1913.

At a hearing of the above entitled appeals, before (95) Hon. C. P. Smith, Member, on September 3, 1930, the following proceedings were had.

Respondent's attorney:

These Strother appeals are allied cases with those of the Bankers Pocahontas Coal Company, and all were determined in the same opinion by the Board. A final order of determination has been entered in the Bankers case, and the Strother appeals were postponed until this was done. Respondent filed its proposed recomputation in the Strother cases, and for the petitioner Strother an alternative computation has been offered, and I suggest for petitioner the objections to the proposed computation of respondent should be stated, and that I be permitted to defend the respondent's proposed computation.

Petitioner's attorney:

These cases of the corporation and of its president and stockholder were heard together. The material problem (96) in the Bankers case being its relation to the

operating companies under certain contracts existing before March 1, 1913. The Board ruled the relation was that of lessor and lessee, and the Bankers Company was entitled to depletion allowances as a lessor of 3.6¢ per ton of coal mined in the several taxable years. The Rule 50 settlement of the Bankers case involved the question whether such decision was proper in fixing coal mined as the basis of depletion, but the determination proposed by respondent was sustained and the deficiencies were entered according to the original opinion. The findings of fact of the Board in these consolidated cases state that petitioner Strother as a stockholder received payments from the Bankers Company which he reported in his return, but did not return them as taxable income. Such amounts were received by the corporation from its operating contracts, and entirely distributed including any depletion reserve. The Commis-
(97) sioner made no allowance to Strother for any depletion reserve so received by him, and added the entire receipts to his net income and determined the deficiency accordingly. The Board opinion says Strother is not taxable upon distributions from the Bankers Company to the extent that same is a distribution of its depletion reserve. The point this morning is that the findings of fact recite all moneys received by the Bankers Company, including depletion reserve, were distributed to its stockholders including Strother, and that the opinion says to the extent of such distribution the depletion received by Strother should be eliminated as non-taxable income the amended computation filed for petitioner Strother applies these findings of fact, assuming that the ratio of depletion reserve received to the entire Bankers income for the taxable period will likewise apply to the amount of the dividend received by the stockholder.

Objection to respondent's proposed determination
(98) was made in the original Strother counter-proposal, and appears deficient because it does not disclose the several steps taken to reach the amount of the proposed deficiency. It has been explained in conference the Department has ascertained the Bankers net income exclusive of depletion and the aliquot amount of same, assuming to represent the tentative daily earnings. Such earnings are computed over the days elapsed with-

in the taxable period until the date of a dividend payment, and to the extent of such earnings the payment is considered as paid from earnings. If the dividend payment exceeds the earnings, the excess is assumed to be a distribution of capital, and if the earnings exceed the dividend, such excess is carried forward to the next dividend date, and the same procedure is had again. When the payments from earnings and from capital are thus determined for an entire year, the proportionate stockholder's interest of Strother in such assumed (99) distribution of capital is ascertained, and is set out in the computation as the amount of his dividend which is taxable. If the determination is to follow the language of the decision and its findings of fact, the determination by respondent introduced other questions which render the findings of fact useless, while the Strother counter-proposal only applies the findings of fact and the decision. In the original counter-proposal an error was made in that the depletion reserve is taken from the adjusted income proposed by the respondent. As such deduction was previously made by respondent, the result is a double deduction for depletion. In the amended counter-proposal, the Bankers net income is compared with the total depletion allowed for the taxable year, and the prorata part which depletion is of net income, is then eliminated from the Bankers dividends and the Strother net income. Adjustment is then made as to the dividend. It is submitted these conclusions (100) follow the findings of fact, and the interpretation of the Board. In conference about the matter, the attorneys have ascertained that depletion allowable under the Board decision to the Bankers Company approximates $125,000 for the years 1920 to 1926 inclusive. At the same time, the distribution of capital under the computation of respondent is about $90,000 and there is accordingly a difference of $35,000 of depletion considered as not distributed. However, the findings of fact say that everything received of the Bankers Company including depletion was distributed. If we follow respondent's method more than 25% of the depletion to which Strother is entitled, is not given to him. For petitioner, a complete counter-computation will be supplied for the year 1919, using the depletion for 1919 determined in the West Virginia litigation, and which

figures were not available when the amended counter-computation was prepared and filed.

Respondent's attorney:

Under the law and rules of practice of this Board, the (101) petitioner who questions a proposed determination of the respondent has the burden to show the correct tax, the correct gross income, the allowable deductions and assumptions, but all this is not done in the greater number of cases. The pleadings pull out of the computation certain elements and an examination is made as to such particular adjustments. In these cases for Strother it was only shown that a certain depletion should be allowed the Bankers Company, out of which a depletion reserve should be established. It is obvious that anything distributed from the depletion reserve to Strother is non-taxable, as a return to him of the capital investment. This record does not show the gross income of Strother for the years in question, nor the facts from which his assumption can be determined. It does not show the natural or taxable character (102) of dividends, or the dividends from other corporations.

There are a number of adjustments in determining the Strother tax in these particular years that no where appear in the record. To make a proper Rule 50 computation, either party must start where the sixty day letter left off as to points not in issue on the appeal. If proof is not made on those points the party must go back and find a basis outside of the Board record as a starting point. Under the laws and regulations it makes a difference in this particular case how a corporation distributes dividends because under the law, it is assumed the corporation first distributes earnings, and until all available earnings for payment of the dividend are distributed, they are taxable at sur-tax rates, and until the earnings are exhausted, there is no distribution of a depletion reserve of other capital. In this case, the dates of payment of the Bankers dividends to Strother and others, were taken into considera-(103) tion by respondent against the earnings of the company as near as they could be found at that time. A sixty day letter was based on such an allocation of

dividends and respondent's present computation assumed that was to be followed. The pleadings raised no question, and no proof was offered in the record of the dates and amounts of dividends and of the earnings of the company, so that the Board itself could prorate them. If the distribution of dividends exceeded the available earnings, there is a necessary automatic capital adjustment to be made without regard to the question of depletion. Respondent believes such adjustment is proper here, and has been used since the first agent's report, and this record supplies no basis for the adjustment. If it is necessary for this record to supply the complete basis for re-computing the Strother tax, the petitioner has failed to maintain the complete burden of proof, but this is not reasonably expected. On the other hand, petitioner cannot now question the necessary (104) and continuous computations which have been in the case from the beginning, and do not drop out of the case where no specific Board finding is made or the record shows no specific evidence on the point. Petitioner's argument is that the depletion determined by the Board for the Bankers Company, instantly became a reserve or capital set aside in place of an exhausted asset, and that as the Board says the corporation entirely distributed its receipts including depletion reserve, it follows Strother is entitled to his entire share of such reserve. This literally follows the word for word decision of the Board. Respondent, however, does not know the Board had anything more in mind than a complete annual distribution of the net of the company. The record shows administration expenses were paid in connection with the collection of these royalties, and that it took and was allowed certain deductions of a business nature, which came out of the income from these operating contracts. Therefore, we know the royalties (105) were not literally and completely distributed, but were used at least in the small administration expenses of the company. In the testimony for petitioner it appears all the royalties were distributed in each year excepting a reserve kept to meet the present question of taxation, and that such reserve will be distributed if no taxes are found due or payable in this litigation. This testimony would justify the Board finding the fact that upon receipt of the royalties the Bankers Company used

what was necessary for ordinary administration expenses, and after setting aside a reserve to meet Federal taxes, distributed the balance to its stockholders. To such state of fact the Board's opinion is applicable in saying that the distribution of the corporation to Strother is non-taxable to the extent same constitutes a distribution of its depletion reserve.

The record does not show the amount of reserve for (106) taxes, but respondent's computation shows a distribution of $20,000 less than the actual distribution, and the total of the proposed deficiencies approximates this amount. In the face of the facts, it is necessary for the Board to revise the findings of fact, and petitioner cannot rely upon the finding of the Board that the Bankers Company distributed all of its depletion, and thereby the stockholders get all of it as non-taxable income.

Petitioner's attorney:

Objection is made to this determination as being one to be decided upon facts other than those established by the findings of fact and opinion of the Board. The opinion discusses entry of judgment under Rule 50. Although the record shows money was being withheld to meet the contingencies of this litigation, it further shows the company is upon a cash basis, and technically has no right to raise a reserve for taxes. That money has (107) been ear-marked for the contingent liability of these taxes, and put in bank, and for practical purposes has been spent toward this litigation, and everything else has been distributed to the stockholders. In such case, the findings of the Board are entirely proper and not open to dispute. They cannot be disputed under this Rule 50 situation, so that means trying the case upon a new cause and new issues, and not upon the decision and finding of fact.

Respondent's attorney:

Subject to verification by the record, the Bankers returns have been introduced in evidence here, and will show a sizable cash balance in bank. This emphasizes that a reserve was set aside, and you cannot have the money in a dividend to Strother, and also in bank in West Virginia as a reserve.

The Member:

The Board in the light of the error pointed out by respondent in its findings of fact, will, of its own motion, (108) amend the last paragraph of the findings promulgated January 22, 1930.

The within Statement of Evidence is hereby approved for certificate and signature by the Board.

CAMDEN R. McATEE
Atty. for Petitioner.

C. M. CHAREST
Atty. for Respondent.

Approved and Ordered filed this 14 day of July, 1931.

CHARLES P. SMITH
Member.

(109) **AGREED PRAECIPE**

Filed July 14, 1931.

UNITED STATES BOARD OF TAX APPEALS

D. J. F. Strother, Petitioner,

vs. Docket Nos. 10472, 25275, 32170

Commissioner of Internal Revenue, Respondent.

The Clerk will please include the following in the record upon the petition of appellant for review of the proceedings of the Board in the above entitled appeals (consolidated) before the United States Circuit Court of Appeals for the Fourth Circuit.

1. Docket entries:

(a) Docket 10472—Complete entries (insert)

(b) Docket 25275—Complete entries through January 22, 1930 followed by statement: "Subsequent docket entries are identical with those in Docket 10472 as appearing herein, and are here omitted."

(c) Docket 32170—Complete entries through January 22, 1930, followed by same statement (as above).

2. Petitions, answers and deficiency letters, as follows:

Docket 10472—Petition
Deficiency letter
Answer

Docket 25275—Caption, followed by statement:

"The petition, and answer are in substance the same (110) as in Docket 10472 and addressed to the same issues herein against adjustments and deficiencies for the calendar years 1922 and 1923, and same are here omitted excepting Paragraphs (b) and (c) of said petition, and the deficiency letter which are as follows:"

Paragraph (b) of petition (insert)

Paragraph (c) of petition (insert)

Deficiency letter (insert)

Docket 32170—Caption, followed by statement:

"The petition and answer are in substance the same as in Docket 25275 and addressed to the same issues herein against the adjustments and deficiencies for the calendar years 1924 and 1925, and same are here omitted excepting the deficiency letter which is as follows:

Deficiency letter (Insert)

3. Board findings and opinion—(January 22, 1930).

4. Petitioner's motion for rehearing and modification (February 27, 1930).

5. Board order denying same (March 6, 1930).

6. Respondent's Rule 50 settlement proposal (March 31, 1930).

7. Board order withholding settlement pending Rule (111) 50 determination in Appeal 14516 (July 15, 1930).

8 (a). Petitioner's objections and Rule 50 counter-proposal (August 12, 1930).

(b) Petitioner's amended Rule 50 counter-proposal (September 2, 1930).

(c) Petitioner's supplemental Rule 50 counter-proposal (September 10, 1930).

9. Board order amending findings (September 26, 1930).

10. Board determination on Rule 50 computation (September 29, 1930).

11. Petition for review.

12. Statement of evidence.

13. Order extending time; orders concerning record contents, not included in record.

14. This praecipe.

(Signed) CAMDEN R. McATEE,
Attorney for Petitioner.

Copy hereof acknowledged; all objections waived and consent record be accordingly prepared.

(Signed) C. M. CHAREST,
Attorney for Respondent.

(112) **AGREED ORDER**

UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

D. J. F. Strother, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent.

(B. T. A. Docket Nos. 10472 25275 32170 Consolidated)

The parties herein by their attorneys having moved the Court for leave by agreed praecipe to establish the record herein before the United States Board of Tax Appeals to be certified for use in this Court as required by its rule, as containing the complete record as to docket entries, pleadings and other proceedings of record in one of the above entitled appeals before said Board, and to establish said record in each of the other appeals as part thereof for use in this Court, complete as to matters pertaining entirely to either of said appeals and by reference as to matters therein which are the same in substance or in identity as in said complete record, and to consider said three appeals consolidated for hearing herein, for cause, that said three appeals before said Board involved substantially the same subject matter, pleadings, proceedings and issues, and (113) were therein heard and decided as a consolidated case and from said decision a single petition for review of said decision has been taken to this Court, and for cause that said records, if established pursuant to the rule of this Court by preparation of a single record in each Board appeal, will be repetitions, confusing and unwieldy, which the parties seek to avoid; and said parties having further moved the Court that, upon filing of the petition for review and record herein and in a related petition for review of Bankers Pocahontas Coal Company in this Court, same shall proceed together as a consolidated case under the separate captions of said proceedings for purposes of briefs, hearing and decision.

And the Court being advised in the premises, it is thereupon considered and ordered:

That *sur* single petition for review filed by petitioner herein before said Board and statement of evidence thereon, the parties shall file with the Clerk of said Board their agreed praecipe to establish the record herein as including the complete record in one of said appeals, as required by rule of this Court, and as including matters from the other appeals pertinent thereto, without repetition of matters appearing in said complete record but with explanatory statements of the substance and reasons for said omissions, and that said three appeals be and the same are considered consolidated and subject to one petition for review and state-
(114) ment of evidence for purposes of said record and hearing in this Court, and that said Clerk of the Board be and he is authorized to certify said record made as herein provided, and that any rule of this Court to the contrary is expressly waived,

And it is further ordered that upon filing in this Court of the petition for review and record herein and in a related petition for review of Bankers Pocahontas Coal Company, that both proceedings shall proceed together herein, but under their separate captions, for purposes of briefs, hearing and decision.

July 8th 1931.

JOHN J. PARKER,
United States Circuit Judge.

Agreed:

(Signed) CAMDEN R. McATEE
Attorney for Petitioner.

(Signed) C. M. CHAREST
Attorney for Respondent.

A true copy.

Teste:

CLAUDE M. DEAN, Clerk,
U. S. Circuit Court of Appeals,
Fourth Circuit.

D. J. F. Strother, Petitioner,

vs.

Docket Nos. 10472, 25275 and 32170

Respondent.

(115) **CERTIFICATE**

I, B. D. Gamble, Clerk of the United States Board of Tax Appeals, do hereby certify that the foregoing pages 1 to 114, inclusive, contain and are a true copy of the transcript of record, papers and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 28th day of July A. D. 1931.

B. D. GAMBLE Clerk.

(SEAL)

PROCEEDINGS IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

No. 3214.

D. J. F. Strother, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

July 29, 1931, the transcript of record is filed and the cause docketed.

Same day, three (3) joint motions to extend the time for the settlement of evidence, and the transmission of the record to this Court are filed.

Same day, order dated February 26, 1931, and signed by John J. Parker, U. S. Circuit Judge, extending the time for a period of sixty (60) days from and after March 3, 1931, within which to settle statement of evidence, prepare the record and transmit same to this Court, is filed.

Same day, order dated April 22, 1931, and signed by John J. Parker, U. S. Circuit Judge, extending the time for a further period of sixty (60) days in addition to sixty days from and after March 3, 1931, granted by order of February 26, 1931, within which to settle statement of evidence, prepare the record and transmit same to this Court, is filed.

Same day, order dated June 25, 1931, and signed by John J. Parker, U. S. Circuit Judge, extending the time for a further period of thirty (30) days in addition to the time granted by orders of February 26, 1931, and April 22, 1931, within which to settle statement of evidence, prepare the record and transmit same to this Court, is filed.

Same day, agreed motion as to the record is filed.

Same day, agreed order as to the record is filed.

Memo. of Clerk: This order is printed at page 90 of the transcript of record.

Same day, the appearance of Camden R. McAtee and Wells Goodykoontz is entered for the petitioner.

August 8, 1931, the appearance of G. A. Youngquist, Assistant Attorney-General, Sewall Key, Special Assistant to the Attorney-General, C. M. Charest, General Counsel, Bureau of Internal Revenue, and D. M. Evans, Special Attorney, Bureau of Internal Revenue, is entered for the respondent.

September 8, 1931, twenty-five copies of the printed record are filed.

October 12, 1931, the originals of petitioner's exhibits numbers 1 and 2 are certified up to this Court.

October 17, 1931, the appearance of Andrew D. Sharpe, Special Assistant to the Attorney-General, is entered for the respondent.

ARGUMENT OF CAUSE.

October 20, 1931 (October term, 1931), cause came on to be heard, together with No. 3215, before Parker and Soper, Circuit Judges, and Baker, District Judge, and is argued by counsel and submitted.

OPINION.

Filed January 25, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS.

FOURTH CIRCUIT.

No. 3214.

D. J. F. Strother, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

No. 3215.

Bankers Pocahontas Coal Company, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

On Petitions to Review the Decisions of the United States Board of Tax Appeals.

(Argued October 20, 1931. Decided January 25, 1932.)

Before PARKER and SOPER, Circuit Judges, and BAKER, District Judge.

CAMDEN R. MCATEE and WELLS GOODYKOONTZ (MASON, SPALDING & MCATEE and GOODYKOONTZ & SLAVEN on brief) for Petitioners, and ANDREW D. SHARPE, Special Assistant to the Attorney General (G. A. YOUNGQUIST, Assistant Attorney General, SEWALL KEY, Special Assistant to the Attorney General, C. M. CHAREST, General Counsel, Bureau of Internal Revenue, and DEWITT M. EVANS, Special Attorney, Bureau of Internal Revenue, on brief) for Respondent.

SOPER, Circuit Judge:

Bankers Pocahontas Coal Company vs. *Commissioner*, No. 3215:

The subject matter of this suit involves income and profit taxes of the Bankers Pocahontas Coal Company for the calendar years 1920-1926, as determined by the Board of Tax Appeals. Deficiencies in substantial amounts were charged against the taxpayer in each of these years; and a petition to review was filed. The Board made the following findings of fact with reference to the property concerned:

"In July, 1912, the Bankers Pocahontas Coal Company, a West Virginia corporation, acquired the fee simple title to approximately 6,200 acres of coal lands, including both the surface and the mineral rights in the State of West Virginia. The land had no appreciable value except for the coal content.

Upon incorporation in 1912, the corporation acquired by formal assignment and has continued to retain the beneficial interest of the original owners in certain contracts affecting the coal content which were executed in 1901 and 1902 with various operating companies and to which contracts the 6,200 acres and coal content were subject.

These contracts were originally prepared by D. J. F. Strother, who at that time was attorney, director and stockholder in the predecessor corporations. The form

of the contracts is that prevailing in the West Virginia coal fields, which followed the Pennsylvania form of contract as introduced by Pennsylvanians who were largely instrumental in the early coal development in the West Virginia field."

Each of these contracts purported to be a contract of lease between the prior owner of the land, as lessor, and a coal mining company, as lessee, covering a tract of land in McDowell County, West Virginia, for a period of thirty years from January 1, 1901. It was provided that the lessee should have the sole and exclusive privilege of mining and coking coal on the premises, and of conducting a general mercantile business thereon. In consideration thereof, the lessee agreed to pay to the lessor, as rental for the premises, a royalty (ranging from 1c to 10c) for each ton of coal mined and sold or used for any other purpose than the manufacture of coke, and a larger amount for each ton of coke manufactured and sold upon the premises. In some cases, a minimum annual rental or royalty (ranging from $4,000 to $10,000) was agreed upon. In addition, the lessee agreed to pay all taxes assessed against the property, or the coal mined, coked or manufactured. The lessee was given the option to renew the lease at its expiration; and provision was made for the final valuation and disposition of the improvements placed upon the land by the lessee.

The contention of the taxpayer is that these contracts, executed in the years 1901 and 1902, and acquired by it in the year 1912, were sales of coal in place that were fully complete before the Sixteenth Amendment went into effect; and that the royalties received during the period 1920 to 1926 were merely payments of obligations that existed unconditionally on March 1, 1913, and were not income taxable under the federal revenue acts. It is said that this construction of mining leases as sales of coal in place is the law of the State of West Virginia, laid down by its highest court, and is therefore a rule of property which the Federal courts must respect and enforce. The Board of Tax Appeals, however, overruled this contention, and directed that the royalties should be included in the gross income of the taxpayer, subject to taxation.

The application of the income tax statutes passed in conformity with the Sixteenth Amendment to the proceeds of mining was first considered by the Supreme Court in *Stanton* vs. *Baltic Mining Co.*, 240 U. S. 103. The court held that a tax on the product of a mine is not, in its essence, a direct tax on property merely because some exhaustion of the ore body must result from the working of the mine; and that even though an adequate allowance is not made for the depletion of the mineral, the tax does not become a direct tax on property because of its ownership. On the contrary, it was held in accordance with its former ruling in *Stratton's Independence* vs. *Howbert*, 231 U. S. 399, that such a tax is a true excise levied on the business of carrying on mining operations. The Supreme Court reiterated and applied this rule in *Von Baumbach* vs. *Sargent Land Co.*, 242 U. S. 503, where it was held that royalties from mining leases on lands in Minnesota constituted income subject to the Corporation Tax Law of 1909. It was pointed out that under the law of Minnesota, such leases are not merely conveyances of the ore in place, and do not constitute a sale of any part of the land, but the ore derived from the operation of the mines constitutes rents and profits from the land. Commenting on this rule, the court said:

"Ordinarily, and as between private parties, there is no question of the duty of the federal court to follow these decisions of the Minnesota Supreme Court, as a rule of real property long established by State decisions. *Kuhn* vs. *Fairmont Coal Co.*, 215 U. S. 349, 360. Whether in considering this federal statute we should be constrained to follow the established law of the State, as contended by the Government, we do not need to determine. The decisive question in this case is whether the payments made as so-called royalties amount to income so as to bring such payments within the scope of the Corporation Tax Act of 1909. The prior decisions of this court in *Stratton's Independence* vs. *Howbert*, 231 U. S. 399, and *Stanton* vs. *Baltic Mining Co.*, 240 U. S. 103, in which the Stratton case was followed and approved, are decisive of this question."

The court also held that there was no difference as

to taxability of the gains from the mining operations, whether the ore was extracted by the mine owner, as in the Stratton case, or by a lessee of the owner, as in the case of the Sargent Land Company.

All of this ground was considered by the Circuit Court of Appeals of the Third Circuit in *Rosenberger* vs. *McCaughn*, 25 F. (2d) 699, a case which related to income taxes based on royalties or rents from coal lands in Pennsylvania. In that State, the courts apply a different rule from that in vogue in Minnesota, and hold that mining leases constitute sales of the mineral in place; and it was therefore argued that the case must be distinguished from the decisions of the Supreme Court we have cited. But it was held, and we think properly, that the rules of decision laid down by the state courts with regard to property, while generally controlling upon the federal courts, do not necessarily govern those courts in the interpretation of the laws of Congress in regard to taxation and, it was pointed out that in *Von Baumbach* vs. *Sargent Land Company, supra*, the Supreme Court had reached the conclusion that royalties from mines constituted taxable income wholly aside from the construction placed by the Minnesota courts upon mining leases. The Supreme Court declined to review this interpretation of its decision when it denied *certiorari*, 278 U. S. 604. See also *Hirschi* vs. *United States*, 67 Ct. Claims 637, *certiorari* denied 280 U. S. 576; *Berg* vs. *Commissioner*, 33 F. (2d) 641, *certiorari* denied 280 U. S. 598; *Burkett* vs. *Commissioner*, 31 F. (2d) 667, *certiorari* denied 280 U. S. 565; *Alexander* vs. *King*, 46 F. (2d) 235.

We shall assume, for the purposes of this decision, that the law of West Virginia, like that of Pennsylvania, is that a mining lease constitutes a sale of the mineral in place. It was said in *Coal Company* vs. *Overholt*, 81 W. Va. 427, 434, that the English and many American decisions hold that when, in a mining lease, the parties contract with reference to a mineral known to exist, the quantity of which is unknown and incapable of exact ascertainment, and the lessee covenants to bring forth a minimum quantity annually, and to pay a minimum royalty, the contract amounts to a sale of the mineral in the land and the lessee is bound to pay the minimum price. See also *Feather* vs. *Baird*, 85 W. Va. 267; *Urp-*

man vs. *Lowther Oil Co.*, 53 W. Va. 501; *Toothman* vs. *Courtney*, 62 W. Va. 167; *Smith* vs. *Root*, 66 W. Va. 633.

Nevertheless, we think that the royalties in question, subject to the deduction allowed by the Acts of Congress, constitute taxable income. There can be no doubt that it was the intention of Congress to tax them. It is provided in Section 234a of each of the pertinent statutes, to-wit, the Revenue Act of 1918, 40 Stat. 1057, the Revenue Act of 1921, 42 Stat. 227, the Revenue Act of 1924, 43 Stat. 253, and the Revenue Act of 1926, 44 Stat. 9, that in computing the net income of a corporation subject to the income tax, in the case of mines and other natural deposits, there shall be allowed as a deduction, a reasonable allowance for depletion, according to the peculiar conditions in each case. It does not follow, as the taxpayer assumes, that the royalties cease to be income under the Acts of Congress because the leases are sales and the royalties are part payment of the purchase price under the law of West Virginia. It is obvious, as the Supreme Court has pointed out, that something more is involved under a mining lease than a sale and delivery of valuable property. Before the business is complete, there must take place the whole process of locating, extracting and preparing the ore for market. This is a manufacturing process, and in this aspect the royalties are seen to be income of the business and as such, subject to taxation. The federal courts must respect the local laws of property laid down by the courts of the state, but the power of Congress to tax must be judged by the realties of the situation and not by the logic of state rules of property, pushed inexorably to their extreme.

In *Weiss* vs. *Wiener*, 279 U. S. 333, the taxpayer, who was in the business of taking long leases on real property and subletting, claimed the right to make an annual deduction from his income for estimated depreciation of the buildings, but the Supreme Court decided that the claim was unfounded since he was not the owner of the property. The court said (p. 337):

"It does not matter that in Ohio, where the properties lie, these long leases are treated as in many respects like conveyances of the fee. The Act of Congress has its own criteria, irrespective of local law, that look to certain rather severe tests of liability and exemption

and that do not allow the deductions demanded whatever the lessees may be called. We understand this to be the view taken by the Department for a long time, and we are of opinion that it should not be disturbed."

It may be noted, in passing, that the Supreme Court of Appeals of West Virginia itself did not apply the rule with regard to mining leases literally when it came to the subject of taxation; for in *Harvey Coal & Coke Co.* vs. *Dillon*, 59 W. Va. 605, it held that a mining lease, similar in all substantial respects to those involved in the pending case, constituted a chattel real, taxable to the lessee under a West Virginia statute which provided for the taxation of personal property, including, in that term, chattels real. This decision was made notwithstanding the contention that the deed created not a chattel real but a sale of the coal itself *in situ*, taxable only as realty.

The taxpayer does not seem to deny the force and effect of the decisions of the Supreme Court we have cited, but claims that the Court has since discarded the theory laid down in these cases and has returned to the well established rule that the state law of property must be accepted and applied by the federal courts. Reference is made to *Tyler, Adm.* vs. *United States*, 281 U. S. 497, *Crooks, Col.* vs. *Harrelson*, 282 U. S. 55, and *Poe, Collector* vs. *Seaborne*, 282 U. S. 101; but it is obvious that each of these decisions turned upon the fundamental question whether the property sought to be taxed came within the purview of the taxing statutes. When it was clear that such was the case, the federal statute was given effect; as in *Tyler* vs. *U. S.*, 281 U. S. 497, where the court held that the value of a tenancy by the entireties should be included in the gross estate of a decedent, for the purpose of computing the tax upon the transfer of the net estate, although, under the state law applicable to such an interest, it could not be said in a strict sense of the term that a transfer of the property had taken place. In the other cited cases, on the other hand, property was held to be excluded from the tax proposed because it did not come within the terms of the statute, and this conclusion was maintained although it was occasioned by observance of a state rule of property, and it was clear that the ruling would bring about a lack of uniformity in the incidence and operation of the tax in

different states by reason of diversity of local property rules. The Supreme Court has never abandoned the rule as to the effect of state decisions on questions of property; but it has held in some instances that state decisions do not cover the whole ground to which the federal taxing statutes relate, and in other instances, that the statutes or decisions of the state lay down rules which define and limit the property which Congress has undertaken to tax.

It is next objected that even if the royalties of the mine are taxable, an insufficient allowance for depletion has been made. The Commissioner estimated the allowance at 3.6c per ton, as the value of the coal in place on the basic date of March 1, 1913; and the deficiencies were determined on this basis. The taxpayer contends that an allowance of 5c per ton should have been made because this sum has been fixed as *res adjudicata* between the parties by reason of a judgment of the District Court of the United States for the Southern District of West Virginia rendered on January 21, 1928. The Commissioner had previously determined a deficiency against the taxpayer for the years 1914 to 1919, using the unit value of 3c per ton, and had imposed additional taxes in the sum of $6,267.08, which the corporation had paid under protest. Thereafter it brought an action against the Collector of Internal Revenue at Parkersburg, West Virginia, wherein the court determined that the rate should be 5c per ton, and rendered a judgment in favor of the taxpayer for $5,373.01, which the United States paid. Hence the taxpayer claims that the question is no longer open between it and the government, since it is a general principle that when a fact is distinctly put in issue, and directly determined by a court of competent jurisdiction between the parties in a law suit as a ground for recovery, it cannot be disputed in a subsequent suit between the same parties or their privies, even if the second suit is for a different cause of action. *Southern Pacific R. R.* vs. *U. S.*, 168 U. S. 1, 48; *New Orleans* vs. *Citizens Bank*, 167 U. S. 371.

The rule is applicable, however, only when the subsequent suit is between the same parties or their privies. The taxpayer maintains that we have that situation in the present litigation because the United States in reality is its opponent in both cases, being represented by the

Collector of Internal Revenue in the prior suit, and by the Commissioner of Internal Revenue now. But the argument is refuted by the decision in *Sage* vs. *United States*, 250 U. S. 33, where it was expressly ruled, against the protest of the government, that the court was not bound by a judgment in a former suit concerning the same subject matter between the taxpayer and a Collector of Internal Revenue, because a suit against a Collector of Internal Revenue is personal and its incidents, such as the nature of the defenses open and the allowance of interest, are different. This ruling has recently been cited with approval by the Supreme Court in *Graham & Foster* vs. *Goodcell*, 282 U. S. 409, 430. The decision of the District Court for the Southern District of West Virginia was therefore not binding upon the Commissioner, and he had the authority to determine anew, as a question of fact, what allowance should be made for the depletion of the mine.

In reviewing the Commissioner's determination, the Board took into consideration not only the evidence introduced before the District Court in the prior case, but also additional evidence. The president of the corporation testified that the cost of the property, when acquired in 1912, did not exceed $507,000, a fact casting strong light on the value of the property on March 1st of the following year; in 1915, an engineer estimated that there were then twenty million tons of mineable coal, having a total value of one million dollars; on December 31, 1917, an entry was made upon the general ledger of the taxpayer that the estimated value as of March 1, 1913, on the basis of twenty million tons of coal at 5c a ton was one million dollars; and the income tax return filed for these years claimed a March 1, 1913, value of the property of one million dollars. A stipulation, filed by the parties before the findings of fact and opinion of the Board were made, to be received as a statement of fact upon any question necessary to any computation under Rule 50 of the Board, contained a schedule showing that the estimated recoverable tonnage on March 1, 1913, was 37,608,642 tons. The stipulation also included a resume of the leases, with the approximate acreage and royalties per ton in each, and also the tonnage mined and royalties received for the years 1913 to 1919 inclusive, as well as the tonnage mined, the tonnage paid for and

the royalties received for the years 1920 to 1926. From this resume of facts, it is obvious that there was substantial evidence to support the finding of the Board. As it pointed out, an allowance of 3.6c per ton would return to the taxpayer a total of $1,353,911.11 upon the tonnage estimated in the stipulation. It is true, as the taxpayer contends, that a different result might have been based upon the evidence in the record; but it is not the province of this court to find the facts anew. We merely ascertained whether there is substantial evidence to support the findings of the Board.

The taxpayer objects to the use by the Board, in determining the depletion rate, of the estimated tonnage in place on March 1, 1913, as shown by the stipulation. It is said that the stipulation was made merely to aid in the computation of the deficiency under Rule 50. The rule is applicable when the Board determines the issues in any proceeding, and withholds decisions of deficiencies for later computation. If the parties are in agreement as to the amount, copies of their computation are filed for entry of the decision; but if not in agreement, the parties may file their respective computations, and an opportunity to be heard is afforded. But any hearing is strictly confined to the consideration of the correct computation, and no argument may be made upon issues or matters disposed of by the report of the Board, or upon any new issues. The stipulation was filed in this case before the time had arrived for the filing of computations under the rule. The Board had not yet determined the principles to be applied in the computation of the deficiencies, and one of the important issues was the rate of depletion to be used in case the royalties should be held to be income. The stipulations of fact were obviously filed by the parties to enable the Board to reach correct conclusions upon the disputed points. We think the Board properly took the stipulated facts into consideration in determining the depletion allowance. They could not justly have been considered for one purpose, and not for others.

After the Board had filed its findings and opinion, the parties filed conflicting computations of deficiency, which then came on for hearing under Rule 50. The taxpayer then for the first time made the point that the schedules filed showed that under two leases, the coal

paid for in several years substantially exceeded the coal mined, and offered to introduce the leases to show that the payments were made as minimum royalties required under the contracts, with leave, to the lessees, at any subsequent time, to take out the coal paid for. The Commission objected to the offer as new matter not receivable at that stage of the proceedings, under the provisions of the rule. The Board decided that the offer constituted in effect a request for rehearing and reargument; and finally filed its order of decision without granting a rehearing or considering the evidence offered. This ruling the taxpayer assigns as error.

It is provided in Regulations 45, 62, 65 and 69, Article 216, that in case a lessee under a mining lease is required to pay annually a specified sum to be applied in payment of royalty for mineral, whenever the same shall be extracted and removed, the value in the ground to the lessor, for purposes of depletion, of the number of units so paid for in advance, will constitute an allowable deduction from the gross income of the year in which the payment shall be made. It would have been proper to have introduced the leases in evidence at the original hearing of the case before the Board had determined the issues involved. But the taxpayer put in evidence only one of the contracts of lease as typical of all the rest. Under this form of lease, the right of the lessee to mine additional coal to offset the excess of royalty paid in any year was limited to the next succeeding year after the amount necessary to produce the minimum royalty for that year had been mined. To such a situation under the facts proved, Article 216 had no relevance. The Board was accordingly correct in its ruling that to receive in evidence the new matter offered by the taxpayer was equivalent to the granting of a rehearing of the case. It was within the sound discretion of the Board to grant or deny the taxpayer's motion; and since the evidence must have been in the possession of the taxpayer from the beginning, we cannot say that the discretion of the Board was abused. *Boggs and Buhl* vs. *Com.*, 34 F. (2d) 859, 861.

Another question for decision relates to the sum of $3,770.40 paid to the corporation in 1924 as damages for an unlawful trespass. The Board made the finding of fact that in 1920, the Flanigan Coal Company, which

owned land adjacent to that of the taxpayer, trespassed on the latter's land and removed coal to which it had no right. It then destroyed the entries and as a result the extent of its operations could not be determined. The situation was discovered in 1923, whereupon the taxpayer brought suit for damages and claimed compensation not only for the coal removed, but also for damages to the property. In 1924 the suit was compromised by the payment mentioned, but this settlement had no relation to the coal extracted as the amount of the same could not be determined. The Board quoted the testimony of the president of the corporation to the effect that the destruction of the entries had absolutely destroyed the method of going into the mine at that point; that he and his engineers had estimated that the damages to the property and to the seam of coal were at least ten thousand dollars; and that $3,770.40 was accepted because the trespasser at the time was in a precarious financial condition.

The Commissioner held that the damages received constituted gross income in the year 1924; that the trespasser had mined or damaged 15,000 tons of coal; and that the taxpayer was entitled to deduct from the amount received the sum of 3.6c per ton, or $540, for depletion. The Board sustained this action. It said that a loss caused by a tortious act, if not compensated for by insurance or otherwise, is deductible from gross income; but that the evidence did not afford facts from which the amount of the loss might be determined; and that the cost of the coal removed by the trespasser or its value on March 1, 1913, was not known. Hence it held that no deduction could be allowed for loss in 1920. As to the year 1924, it made the following statement:

"The same situation obtains with respect to the year 1924. The company received from the trespasser $3,770.40. The petitioner has found that all but $540 of this amount (which he has allowed as a deduction from gross income as depletion) constituted taxable income of the company for 1924. The company has submitted no evidence that the cost or March 1, 1913, value of the coal removed by the trespasser was in excess of $540 or that such basis plus damages to the property was in excess of $540. The determination of the Commissioner

is therefore sustained for lack of evidence showing error on the part of the respondent."

The taxpayer objects to this addition to its income for the year 1924, on the ground that the money paid by the trespasser was merely compensation for injury to the mine, and was in effect a return of capital. Any loss or gain in the transaction could be determined under the circumstances only upon a final disposition of the property. We think this position is sound. If the taxpayer were asking for a deduction from income in 1920 for the loss caused by the trespass in that year, it would be within the province of the Board to determine whether the evidence submitted by the taxpayer was sufficiently definite to justify the allowance claimed. The finding of the Board, that the amount of the coal removed could not be ascertained, showed that the amount of the loss was uncertain. But this finding likewise shows that the Commissioner's action in adding the sum of $3,770.40 to the gross income of the taxpayer in 1924, was without foundation. If there had been substantial evidence to support the finding that 15,000 tons of coal had been unlawfully extracted, and that $3,770.40 had been paid solely in settlement of that wrong, it would have been proper to have added this amount to the gross income, less the expenses for collection and an allowance for depletion. The balance remaining would have been as clearly profit in the taxpayer's hands as if it had been paid by a lessee operating on a royalty basis. But the situation is confused by the fact that the amount of coal extracted is not known. So far as can be told from the record, the amount paid by the trespasser may not have exceeded payment at the rate of 3.5c per ton. In addition, there is the uncontradicted evidence of substantial damage to the approach to the mine.

These circumstances show that the Commissioner was not warranted in adding the sum of $3,770.40, less an estimated depletion allowance of $540 to the corporation's taxable income for the year 1924. We are not dealing with a situation like that considered by the Supreme Court in *Burnet* vs. *Sanford & Brooks Co.*, 282 U. S. 389, but with a loss of capital investment. In *Doyle* vs. *Mitchell*, 2447 U. S. 179, 185, the court, speaking of such a question, said: "In order to determine whether

there has been a gain or loss, and the amount of gain, if any, we must withdraw from the gross proceeds an amount sufficient to restore the capital value that existed at the commencement of the period under consideration." A taxpayer is not allowed to deduct a loss from gross income until the amount is definitely fixed and ascertained; and for the same reason, he should not be charged with gain on pure conjecture unsupported by any foundation of ascertainable fact. See *Burnet* vs. *Logan*, 283 U. S. 404.

It follows that as to the determination of the deficiencies of the corporation for all of the years in question except the year 1924, the action of the Board is affirmed, and as to that year, the case is remanded for further proceedings in accordance with this opinion.

Strother, Petitioner, vs. *Commissioner of Internal Revenue,* No. 3214.

This case relates to the income of a stockholder of the Bankers Pocahontas Coal Company derived from dividends by which the greater part of the royalties which the corporation received, were distributed. During the several years involved in the foregoing case, 1920 to 1926, Strother, as one of the corporation's stockholders, received dividend payments from the company and reported them in his income tax returns, but did not return them as taxable income. The Board found, in its original findings of fact, that the corporation made distribution of the entire amounts received by it as royalties, including any depletion reserve. The Commissioner determined as deficiencies against Strother the total amounts received by him from the company, and made no allowance for that part of the moneys which constituted depletion of the capital. Upon these facts, the Board held in its opinion that to the extent that the distribution made by the corporation constituted a distribution of depletion reserve, the amount received by Strother was non-taxable.

The opinion established, as we have seen, that the royalties constituted income to the corporation, and not the proceeds of sale of mineral in place, and that the proper allowance for a depletion reserve was at the rate

of 3.6c per ton. By stipulation of the parties, the decision on these matters was adopted in the Strother case. After the decision was rendered, a hearing was held upon the recomputation of the Strother deficiencies. Strother objected to the new computation proposed by the Commissioner because it did not provide for the deduction from the dividends received of a proportionate part of the entire allowance for depletion. It seems that the total depletion allowance of the corporation for the years in question was $125,000, but the computation was made as if the total allowance was only $90,000. Apparently, the Commissioner held that a sum retained by the corporation in each year to meet the tax deficiency, was in fact part of the allowance for depletion, and to that extent. the allowance for depletion had not been included in the dividends. Another question seemingly involved was whether or not in determining how much of the dividends were capital, the total net income and the total depletion for the year should be pro rated to the date of each dividend payment.

These questions appear to be those which are raised by the petitioner; but the record in the case is so vague that we cannot obtain a clear conception either of the facts to be considered or the questions of law to be decided. This situation doubtless arose because the important questions in which the parties were interested were those concerning the character of the royalty payments as return of capital or income, and if income, the proper allowance to be made on account of depletion. A decision could not be reached in the Strother case until these questions had been determined. At the hearing on the question of recomputation of the Strother deficiencies, it was pointed out by counsel for the Commissioner that the record did not supply a complete basis for recomputing the Strother tax; that, strictly speaking, the taxpayer had failed to maintain the complete burden of proof, but that this was not reasonably to be expected under the circumstances. It was conceded that the recomputation proposed by counsel for Strother was literally in compliance with the decision of the Board, but that this decision was in need of revision. Thereupon, the Board announced that it would make an amendment of its findings of fact, and this was filed after the hearing. Instead of the statement that the corporation distributed

the entire amount received from its operating contracts, the finding was substituted that the corporation used such portion of the royalties as was necessary for the payment of administration expenses, set aside a certain reserve to meet the federal taxes, and distributed the rest to the stockholders. No change was made in the opinion as to the holding that to the extent the amounts received by Strother included depletion reserve, they were not taxable; and without further recomputation, the decision complained of was promptly entered.

The government's brief in the case before us suggests that the record does not contain sufficient facts to permit a determination of the questions raised, and that therefore the Board's decision should not be disturbed. We think, however, that under the circumstances, it would be just for the Board to give further consideration to the Strother case, and to afford to the taxpayer an opportunity to introduce additional testimony to bring out the facts necessary to a decision of the issues involved. The case will therefore be remanded for further proceedings in accordance with the opinion in the case of *Bankers Pocahontas Coal Company* vs. *Commissioner*, insofar as it determines the questions involved herein, and without prejudice to the right of petitioner to rely upon the legal positions as to other matters urged upon this appeal.

Case No. 3214, *Remanded for further proceedings.*
Case No. 3215, *Modified.*

JUDGMENT.

Filed and Entered January 27, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS.
FOURTH CIRCUIT.

No. 3214.

D. J. F. Strother, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

THIS CAUSE came on to be heard on the transcript of the record from the United States Board of Tax Appeals, and was argued by counsel.

ON CONSIDERATION WHEREOF, It is now here ordered and adjudged by this Court that this cause be, and the same is hereby, remanded to the said United States Board of Tax Appeals for further proceedings in accordance with the opinion of this Court in case No. 3215, *Bankers Pocahontas Coal Company versus Commissioner of Internal Revenue*, in so far as it determines the questions involved herein, and without prejudice to the right of petitioner to rely upon the legal positions as to other matters urged upon this appeal, in accordance with the opinion of the Court filed herein.

MORRIS A. SOPER,
U. S. Circuit Judge.

January 27, 1932.

February 8, 1932, petition of petitioner for a stay of the mandate is filed.

Same day, order staying the mandate is filed.

PETITION OF PETITIONER FOR A REHEARING.

Presented February 26, 1932.

(Style of Court and Title omitted.)

Come the petitioners herein by their attorneys, and move the Court for a reargument of the cases presented, and a rehearing of the Court's decision of January 25, 1932, particularly for the reasons and causes herein specifically stated, as well as others apparent on the records, and to be amplified by reargument and rehearing.

The respondent taxgatherer proposes to assess and levy the taxes in controversy solely as taxes upon income authorized by the XVI Amendment, and imposed under the several Revenue Acts which give effect to said Amendment.

The petitioning taxpayers herein protest against said assessment and levy on the ground that said income taxes are neither authorized by the XVI Amendment, nor imposed by the various Revenue Acts.

A citizen may owe a tax as of right, but under the law he may not owe same. In case of doubt whether a tax is owing, the citizen may claim the benefit of the doubt.

In support of the present motion, petitioners respectfully would show the Court has erred as follows (error indicated by black face type):

(1) This Court holds:

> The certain instruments executed in 1901 by a land-owner (whose resulting interest was acquired by petitioner corporation in 1912), granting the exclusive right to mine the coal-content from said land until exhausted in consideration of payment by the grantee of a fixed amount per ton mined each year, and of a fixed minimum annual payment, effected sales of coal in place under the Laws of West Virginia where the lands are situate; **that the payments**

receivable by the grantor (or its assignee) pursuant to said instruments in the several years, are royalties, which Congress intended to subject to income tax under the several Revenue Acts enacted pursuant to the XVI Amendment after deduction therefrom of the depletion allowances provided by said Acts as available to a lessor.

The definite errors are:

(a) By said sale in place, as effected before the enactment of the XVI Amendment on March 1, 1913, was created the right to recover or collect the purchase money in the ensuing years before and after said date and said payments, whether called royalties or not, when received after said basic date are not taxable income in whole or in part.

(b) The Congress has only allowed depletion to the owner of an interest in the depletable property, including lessor and lessee, and has not allowed nor intended to allow depletion to a vendor who has parted with interest in the property.

(c) The Revenue Acts make other provisions for determination of the taxable profit of a vendor.

(d) This Court has wrongly applied the law to the facts of the case.

(2) This Court holds:

That the depletion rate of 3.6 cents per ton is applicable to coal mined, and not to coal paid for but not mined whereby the payments, as to the excess of any payment over the part thereof determined by the quantity of coal mined, is not subject to any depletion allowance.

The error is:

(a) The depletion unit, being premised upon the expectancy of entire annual minimum payments, should apply to coal paid for instead of coal mined in the several years.

(b) The Courts have reversed the position of the Board as herein substantially adopted by this Court.

ARGUMENT.

These points of decision are argued here because if the error alleged in the first be admitted, the second is immaterial. In presenting the cases, the parties were in conflict as to the construction of the instruments under the West Virginia precedents, petitioner contending they effected sales in place, and respondent contending they were only leases. The parties were not in conflict that the West Virginia rule, whatever the Court found it to be, was decisive of the liability of the payments to tax. In view of the uncertainty whether a sale in place was effected, petitioners before the Board and before this Court, were obliged to argue the sufficiency of the depletion allowance as the alternative arising for decision if there was no sale in place. When a sale in place is established the amount of depletion becomes immaterial, as that issue is removed from the case. The vendor who has parted with the depreciable property can have no depletion allowance against its sales proceeds, under the Revenue Acts.

Now, that this Court specifically holds the instruments effected sales of coal in place, the path is straightened toward final and correct determination of the rights of the parties under the XVI Amendment and several Revenue Acts. In addition to the grounds given in the opinion for holding a sale in place was effected, specific reference to the instruments strengthens said conclusion. It appears, that the vendor owner covenants the purchaser of the coal content "*shall have quiet and peaceful enjoyment of same*" (the certain tract of land), thus giving the purchaser *control* and *possession* of the whole tract; the vendor owner further gives the purchaser "*the privilege* of using so much of the surface of said land, and so much of the lumber, stone, sand, clay and water *as may be necessary*", thus evidencing the intent of making a severance of realty, and giving entire possession for

benefit of the purchaser from any dominion, control or possession by the vendor owner. The interpretation of these unique and unusual provisions is controlled by the manifest intentions of the parties, and is but little influenced by other contracts of a like general nature, but lacking such direct contractual provisions, and leads inevitably to the conclusion that a sale in place was intended and effected.

This brings us to the discussion of the specific errors above alleged:

> **1(a) By said sale in place, as effected before the enactment of the XVI Amendment on March 1, 1913, was created the right to recover or collect the purchase money in the ensuing years before and after said date and said payments whether called royalties or not, when received after said basic date were no more taxable income than were the payments of same received before said date.**

The XVI Amendment, says Mr. Chief Justice White in *Stanton v. Baltic Mining Co.*, 240 U. S. 103:

> *"conferred no new power of taxation"*—

In his earlier opinion in *Brushaber v. Union P. R. Co.*, 240 U. S. 1, Judge White pointed out that Congress was invested by the Constitution with every conceivable power of taxation, subject to provisions thereof that direct taxes should be apportioned and indirect taxes should be uniform, and that the income taxes of the Civil War were classed as indirect taxes.

The opinion explains the XVI Amendment became necessary to remove the principle enunciated in the *Pollock* case (157 U. S. 429), that a tax upon income enacted as an excise tax subject to the rule of uniformity was a charge upon invested property, and, to that extent, was a direct tax requiring apportionment, and consequently unconstitutional.

In *Evans v. Gore*, 253 U. S. 245, the genesis of the XVI Amendment is reviewed together with intervening precedents, as a basis for conclusion that same did not extend the taxing power to new or excepted subjects. Reference is made in the opinion to the message of Governor Hughes to the New York Legislature, expressing the fear that same might extend to excepted subjects, and to the assurances to the contrary thereby obtained.

As the XVI Amendment does not add to the power of Congress to tax, and merely struck down the *Pollock* principle, as said in the *Baltic Mining* case in that it

> —"simply prohibited the previous complete and plenary power of income taxation possessed by Congress from the beginning from being taken out of the category of indirect taxation to which it inherently belonged, and being placed in the category of direct taxation subject to apportionment by a consideration of the sources from which the income was derived"—

it follows the XVI Amendment authorizes no income tax upon a claim accrued before and existing on March 1, 1913, when subsequently recovered or collected. The proposition states itself and is a mirror for our argument. Such a claim was capital, and the realization of its subsequent proceeds remains as capital. Thus in *Burnet v. Logan*, 283 U. S. 404, taxpayer after March 1, 1913, sold certain stock for a consideration payable in cash and in the receipt of certain royalties upon ore subsequently mined. It is held she received no taxable income in the payment to her of the royalties, until and after such payments had returned to her the value of her stock when same was sold, and that any attempt to state a partial capital return by depletion calculations would be and is a determination of income by mere conjecture not available to respondent, and not to be imposed on taxpayer.

In the present case for example, the receipts including the years in controversy since March 1, 1913, total $750,000 which is less than the $1,000,000 value in 1913 which the Board and Court says will be returned to the extent of $1,300,000 upon exhaustion of the mines. It follows said capital value of 1913 has not been received, and that no income is contained in the annual payments. If there be no income, the entire receipt is a return of capital.

Test it as you will, the annual receipt of payments of the purchase price for the sale of coal in place is the return merely of capital without income increment.

1(b) The Congress has only allowed depletion to the owner of an interest in the depletable property, including lessor and lessee, and has not allowed nor intended to allow depletion to a vendor who has parted with interest in the property.

If this proposition is correct, it is not necessary to argue for the weight that Congress may or may not give to state rules of property in levying the income tax. That Congress must and does recognize the state rules of property becomes self-evident.

In *Stanton* v. *Baltic Mining Co.*, 240 U. S. 103, and *Burnet, Commissioner, v. Thompson Oil and Gas Co.*, 283 U. S. 301, the rule is definitely stated that a taxpayer is not entitled as a matter of right to make any deduction from annual income for depletion, and authority therefor must be found in the Revenue Acts. The several Revenue Acts allow the prescribed deduction to an owner, and to lessor and lessee, by equitable apportionment of same between them. The deduction is not allowed otherwise, and the right to it is strictly construed. Thus the *Thompson Oil* decision denies any increase in the depletion deductions for later years to redress the apparent inadequacy of deductions previously permitted. In *Darby Lynde Co. v. Commissioner*, 51 F. (2) 32 (C. C. A. 10) (cert. denied, 52 S. C. 40), the de-

pletion on discovery value available to a partnership is denied to a successor corporation created and owned by the partners. In *Pugh v. Commissioner,* 49 F. (2) 76 (C. C. A. 5) (cert. denied, 52 S. C. 22), the taxpayer is held upon conveyance by him of his interest in a mineral lease to thereby lose the right to depletion as to said interest, the ground being he has become a lessee without investment. In *South Vernon Oil Co. v. Hopkins,* 49 F. (2) 1028 (C. C. A. 5), the conclusion is the same, notwithstanding the Revenue Act of 1926 defines allowable depletion as a fixed per cent of gross income from the property during the taxable year, on the ground the sale severed the depletable interest in the property. In *Fleming v. Commissioner,* 6 B. T. A. 900, affirmed 50 F. (2) 1075 (C. C. A. 9), the life beneficiaries under trusts are held not entitled to depletion against trust income consisting of royalties from ore properties. In *Murphy Oil Co. v. Burnet, Commissioner,* —F. (2) — (January 11, 1932) (C. C. A. 9), the Court describes the statute:

> "The Statute with reference to depletion of oil properties is a special one with reference to the particular subject of oil leases involving the production of oil and minerals from mines, and the consequent return of capital by the owners of interests therein, and controls over other general provisions of the law in regard to the return of capital investments."

In *Weiss v. Wiener,* 279 U. S. 333, as this Court says: The depreciation upon buildings contended for by taxpayer was disallowed notwithstanding his long lease savored of a fee under the laws of Ohio, because:

> "The Act of Congress has its own criteria, irrespective of local law, that look to certain rather severe tests of liability and exemption and that do not allow the deductions demanded whatever the leases may be called"—

which is a reiteration of the fact of the case, stated in the opinion as follows:

> —"he must show an interest in the property and a present loss to make the statute apply."

Mr. Justice Holmes correctly finds Wiener as lessor was merely renting the property and improvements, and being without interest therein, had no right to the depreciation allowance prescribed in the Revenue Act. In so doing, reference is made to *Lynch v. Allworth Stevens Co.*, 267 U. S. 364, where a lessee is declared entitled to depletion, although without title to the ore deposit, since the right to remove the ore is a property right which decreases as the mine is exhausted. There is no decision that the so-called lessor remains a lessor after parting with title to the mineral. We do not believe this Court intended to lay down that unique proposition of law in its opinion, but such is its effect.

Admitting the "Act of Congress has its own *criteria*, irrespective of local laws", it appears *interest in the depreciable or depletable property* is part thereof, and that in case of severance of the interest, or failure to acquire the interest, the taxpayer has no right to depreciation or depletion. But the Act of Congress does not prescribe the *criteria* of severance, and same must be found in the local law. If the discoverer of mineral conveys same he loses his right to depletion, and his purchaser does not acquire the right to deplete upon a discovery value. If the lessor sells his royalty interest, or the lessee sells his contract interest, each loses the right to depletion. If an owner sells coal in place, the right to depletion passes to the purchaser and cannot be forced upon the vendor by the decision of this Court when not authorized by the Revenue Acts.

That the *criteria* of severance is derived from the local law appears in *Group One Oil Corporation*, 283 U. S.

279, where the local law of sale of mineral in place was held to divest the property of its previous immunity from tax. We point out other instances hereafter.

We have said it was not necessary to argue the weight to be given to local laws of property by Congress to sustain the present proposition. We are here dealing with real property and the position of Congress and of the Courts in that such rules must be recognized and given effect.

In *McCormick v. Sullivant*, 10 Wheat. 192, we read:

> "It is an acknowledged principle of law, that the title and disposition of real property is exclusively subject to the laws of the country where it is situated, which alone can prescribe the mode by which a title to it can pass from one person to another."

In *United States v. Fox*, 4 Otto 315, we read:

> "The power of the State to regulate the tenure of real property within her limits, and the modes of its acquisition and transfer, and the rules of its descent, and the extent to which a testamentary disposition of it may be exercised by its owners, is undoubted. It is an established principle of law, everywhere recognized, arising from the necessity of the case, that the disposition of immovable property, whether by deed, descent or any other mode, is exclusively subject to the government within whose jurisdiction the property is situated. *McCormick v. Sullivant*, 10 Wheat. 202. The power of the State in this respect follows from her sovereignty within her limits, as to all matters over which jurisdiction has not been expressly or by necessary implication transferred to the Federal Government. The title and modes of disposition of real property within the State, whether *inter vivos* or testamentary, are not matters placed under the control of Federal authority. Such control would be foreign to the purposes for which the Federal Government was created, and would seriously embarrass the landed interests of the State."

As the sale in place made the owner and corporate petitioner (its successor), a vendor, Congress, through income tax taxation or otherwise, could not treat such vendor as a lessor. The proceeds of the sale in place became purchase money not rentals under a lease, and they so remain. If A owned no property he is not taxable as an owner, vendor or lessor, or if he leased his property he is not taxable as a vendor, or if he sold it he is not taxable as a lessor. As said in *Nichols v. Coolidge*, 274 U. S. 531:

> "—under the mere guise of reaching something within its powers, Congress may not lay a charge upon what is beyond them. Taxes are very real things and statutes imposing them are estimated by practical results."

1(c) The Revenue Acts make other provisions for determination of the taxable profit of a vendor.

Only a few pertinent decisions are given in support of this proposition for the sake of brevity. In *Ferguson v. Commissioner*, 45 F. (2) 573, (C. C. A., 5), taxpayer in Texas negotiated oil leases as to 7/8ths of the mineral, retaining the remaining 1/8th interest, and received thereby a cash bonus and the royalties. Under the laws of Texas he made a sale in place of the 7/8ths interest, and his bonus-receipt was held subject to the Revenue Act provision imposing a special rate of tax upon the bonus as a capital gain from a sale, and his retained interest was held subject to depletion allowances as a property interest retained by him.

In *Alexander v. King*, 46 F. (2) 235, a taxpayer in Oklahoma claimed her royalty receipts described as "the equal 1/8th of all oil produced and saved" were subject to the capital gain provision. But in Oklahoma there can be no ownership of oil in place, and consequently no

sale of same, and consequently the capital gain provision was inapplicable as there was no sale.

In *Berg v. Commissioner*, 33 F. (2) 641 (C. C. A. of D. of C.) and *Burkett v. Commissioner*, 31 F. (2) 667, responding to the contention that the capital gain provision should apply, it was held the instruments did not effect a sale and the provision could not be invoked.

Herein, where this Court finds a sale in place of the entire coal content, it follows, under the *Ferguson* case, that the profit, if any, is subject to be ascertained under the capital gain provision and not under the depletion provision of the Revenue Acts. But neither applies until the receipts have returned the capital value sold, and we have shown such return is not yet accomplished.

1(d) This Court has wrongly applied the law to the facts of the case.

This Court concludes, after discussion of various judicial precedents, that the several instruments effected sales of coal in place, and, nevertheless, the payments receivable as the proceeds of said sales, subject to depletion allowances, constitute taxable income, saying:

> "The Supreme Court has never abandoned the rule as to the effect of State decisions on questions of property; but it has held in some instances that State decisions do not cover the whole ground to which the Federal taxing statutes relate; and, in other instances that the statutes or decisions of the State lay down rules which define the property which Congress has undertaken to tax."

Respectfully, this conclusion is provoking in its indefinite statement. The Federal taxing statutes, as in the *Tyler* case, deal with a succession or transfer tax or death duty laid upon the happening of an event as distinguished from its tangible fruits; or they deal with a tax upon the tangible fruits, that is the taxable income,

if any, realized from a transaction. In either case, the tax springs into existence upon the happening of an event. In case of income tax laws, as Mr. Justice Holmes says in *Weiss v. Wiener, supra*:

> "They do not charge for appreciation of property * * * unless realized in money by a sale."

Having a sale in the present case, as the only material factor, we do not believe this Court intends to say:

> "—it (the Supreme Court) has held in *cases of a sale* that state decisions do not cover the whole ground to which the *income tax* statutes relate; and in other *cases of a sale* that the statutes or decisions of the state lay down rules which define the property which Congress has undertaken to tax."

for if that is its meaning, we cannot apply the rule as any decision of the present case.

The coal-lands herein undoubtedly represented a capital asset, the sale of any part of which might be made, but the Revenue Acts nowhere define a sale. The Supreme Court has defined a sale as:

> "Ordinarily a transfer of property for a fixed price in money or its equivalent." *Five Per Cent Cases*, 110 U. S. 471.
>
> "Sale is a word of precise legal import both at law and equity. It means at all times, a contract between the parties, to give and to pass rights of property for money—which the buyer pays or promises to pay the seller for the thing bought and sold." *Williamson v. Berry*, 8 How. 495, 544.

As the word "sale" has an universal meaning, and as real property interests were sold in this case, in the absence of its definition in the Revenue Acts, resort must be had to the laws of West Virginia to determine the interest or title conveyed by the instruments, and this

Court finds a sale in place was thereby made in 1901. It follows the vendor was thereby divested of ownership and interest, and that no interest is available for depletion allowances.

This Court refers to mining as a business and to royalties as income from same, and therefore subject to taxation. This is derived from *Strattons Independence v. Howbert,* 231 U. S. 399, rejecting the contention that:

> "—a mining corporation is not engaged in business, properly speaking, but is merely occupied in converting its capital assets from one form into another"—

but in that case the distinction applicable to this case is clearly stated:

> "The sale outright of a mining property might fairly be described as a mere conversion of the capital from land into money."

Having sold the coal content for money, herein the original vendor and its successor thereafter had no mine, no interest in a mining business, nothing but a claim for the purchase price as the result of conversion of its capital from land into money.

In *Stanton v. Baltic Mining Co.,* 240 U. S. 103, it is true the *Stratton* case was followed, but that does not make either decisive herein. In both those cases, the taxpayer was "*carrying on mining operations * * * upon mining lands owned by itself*", and engaged in a manufacturing process. In the *Stanton* case, it was contended the income tax fell upon the property and was prohibited by the Pollock rule; it was decided the XVI Amendment destroyed the Pollock precedent, and that as an excise tax same was not a direct tax upon property.

In *Von Baumbach v. Sargent Land Co.,* 242 U. S. 503, quoted by the Court, the situation is summarized in the opinion as follows:

"We think that the payments made by the lessees to the corporations now before the Court were *not in substance the proceeds of an outright* sale of a mining property, but, in *view of the terms of these instruments, were in fact rents or royalties* to be paid upon entering into the premises and discovering, developing and removing the mineral resources thereof, and, as such, must be held now as then, to come fairly within the term 'income' as intended to be reached and taxed under the terms of the Corporation Tax Act." (Our italics.)

To complete our argument we cite *United States v. Biwabik M. Co.*, 247 U. S. 116, in which a lessee in Minnesota of iron ores is held, upon authority of the *Sargent* case to be *"in no legal sense a purchaser of ore in place"*, and not entitled to any depletion. By the *Sargent* case (the lessor) and the *Biwabik* case (the lessee), it appears neither lessor nor lessee was entitled to any depreciation under the Act of 1909, and, in *Lynch v. Alworth Stevens Co.*, 267 U. S. 364, this is plainly stated. The Revenue Act of 1916, however, provided a deduction for "exhaustion of property arising out of its use", and the *Lynch* case held same was not available alone to the lessor as the holder of title, but was available also to a lessee who had no title to the ore in place. This conclusion is placed on the ground that the right of the lessee to mine and remove the ore is property within the meaning of the statute.

In these authorities there is no direct definition of the depletion rights applicable to *proceeds of an outright sale*, but a distinction between such *proceeds* and mere *royalties* or rentals is evident. The Court carefully defines the receipts as not *proceeds of a sale*, or characterizes the taxpayer as *not a purchaser*, or as *with or without an interest* in the ore in place.

Hirschi v. United States, 67 Ct. Cl.; *Berg v. Commissioner*, 33 F. (2) 641, and *Burkett v. Commissioner*, 31

F. (2) 667, have some authority when the denial of certiorari is suggested. But the *Burkett* and *Berg* instruments do not appear to be more than leases and the decisions become immaterial. The *Hirschi* instrument is held not effective as a sale in place under the laws of Texas and the Court supports same by citation of *Steedman v. United States*, wherein certiorari was denied, but the *Steedman* case is expressly disapproved in *Crooks v. Harrelson*, 282 U. S. 55. The *Hirschi* case is in effect disapproved in *Group One Oil Corporation v. Bass*, 283 U. S. 279. The Court of Claims says in the Hirschi decision:

> "Congress in passing a revenue act does not, and is not called upon to suit the revenue system of the country to the varying and conflicting decisions and laws of the different states."

But in the later decision of *Poe, Collector, v. Seaborn*, 282 U. S. 101, the Supreme Court said:

> "These Sections (of the several Revenue Acts) lay a tax upon the net income of every individual. The Act goes no further, and furnishes no other standard or definition of what constitutes an individual's income. The use of the word 'of' denotes ownership. It would be a strained construction, which, in the absence of further definition by Congress, should impute a broader significance to the phrase." * * *
>
> "Said differences of state law, which bring a person within or without the category designated by Congress as taxable may not be read into the Revenue Act to spell out a lack of uniformity."

If the proceeds of a sale in place are not taxable when ascertained by the law of West Virginia, but, as proceeds of a lease, are taxable in another state, the return

not subject to taxation in either case is the depletion allowance against same intended to return the capital outlay. There is no lack of uniformity for the vendee of the mineral in place taxes the entire depletion deduction, while lessor and lessee divide same between them.

If the rule be that, notwithstanding a sale in place, the vendor is entitled to depletion, same conflicts with the established rule that depletion follows the property interest. It means the sole owner of the capital interest is partially deprived of the depletion deduction. It means a denial of final decisions to the contrary, and an allowance not authorized by law. It means confusion for the annual payments by the vendee are, as to him, capital investments not deductible from his gross income, *Jefferson Gas Coal Co. v. Commissioner,* 52 F. (2) 120 (C. C. A., 3), and as to the vendor they are rentals and not purchase-money receipts.

Rosenberger v. McCaughn, 25 F. (2) 699, is not rested upon the Supreme Court decisions in prior cases, but upon the ground that the calculation of income by the Commissioner as being within the payments received as proceeds of a sale in place is nowhere questioned and upon the ground—

> "—we think each payment represented in some measure both capital and increment, capital because it stood in the place of coal, and increment because in the payments running through ninety-nine years interest on the capital must inevitably have been included." * * *

This thought of the Court contravenes the settled rule stated with copious citation in *United States v. Merriam,* 263 U. S. 179:

> "On behalf of the government it is urged that taxation is a practical matter, and concerns itself

with the substance of the thing upon which the tax is imposed, rather than with legal forms and expressions. But in statutes *levying taxes the literal meaning* of the words employed is most important, for such statutes are not to be *extended by implication* beyond the clear import of the language used. If the words are *doubtful*, the *doubt* must be *resolved against* the government and *in favor of the taxpare* * * * ."

"I am not at all sure that in a case of this kind—a fiscal case—form is not amply sufficient; because as I understand the principle of all fiscal legislation, it is this: If the person sought to be taxed comes *within the letter of the law, he must be taxed*, however great the hardship may appear to the judicial mind to be. On the other hand, if the Crown, seeking to recover the tax, *cannot bring the subject within the letter of the law, the subject is free, however, apparently within the spirit of the law the case might otherwise appear to be. In other words, if there be admissible in any statute what is called an equitable construction, certainly such a construction is not admissible in a taxing statute*, when you can simply adhere to the words of the statute."

It contradicts *Saunders v. Commissioner*, 29 F. (2) 832 (C. C. A., 3); *Platt v. Bowers*, 13 F. (2) 951; *United States v. Guinzberg*, 278 F. 363 (C. C. A., 2); *Park v. Gilligan*, 293 F. 129, and *Schneider v. Duffy*, 43 F. (2) 642, previously discussed in the brief of petitioners. It contradicts *Logan v. Commissioner*, 42 F. (2) 193 (C. C. A., 2), as recently affirmed in *Burnet v. Logan*, 283 U. S. 404. These are decisions that subsequent payments upon rights to money established and accrued before the XVI Amendment are only the return and collection of capital without income increment.

From these several viewpoints, we submit the Court has not applied the precedents properly because same, under the different facts of this case, and under subsequent *stare decisis*, are inapplicable to the present case.

2(a) The depletion unit, being premised upon the expectancy of entire annual minimum payments, should apply to coal paid for instead of coal mined in the several years.

(b) The Courts have reversed the position of the Board as herein substantially adopted by this Court.

These points relate to the alternative position that depletion is allowable herein.

The Board ruling and the approved tax determination allow depletion only upon coal mined in any year instead of upon coal actually paid for. In presenting its tax determination so approved, respondent's counsel (R. 108) stated apologetically to the Board:

> "—in the respondent's computation allowances were computed at the rate of 3.6 cents per ton upon tonnage mined each year; that this method was in accordance with the opinion in this case, and consistent with the Board's rulings in other cases, *although the respondent in other cases was committed to the principle of allowing depletion on tonnage of coal paid for instead of upon tonnage actually mined in a taxable year.*" (Italics ours.)

The struggle of the Board against the position of respondent and taxpayers that depletion is allowable upon coal paid for and not merely upon coal mined, which would include depletion on any bonus or payment in excess of the price of coal mined, did not reach the courts for a long time, and when it did the Board was recently reversed in *Murphy Oil Co. v. Burnet*, — F. (2) — (January 11, 1932) (C. C. A. 9).

Therein, respondent, by cross-petition, carried the issue to the Court, and obtained a most thorough and convincing opinion upon the question.

In the present case, the Board set out in its findings certain schedules of production and royalty payments, which this Court has approved. Petitioner (R. 109) sub-

mitted same demonstrated the minimum payments substantially exceeded the payment for coal mined, and offered to confirm the fact by the instruments themselves. The refusal of the Board to allow depletion upon coal paid for is a specific assignment of error.

The materiality of the question arises in three ways:

First. If petitioner receives $200 as a 10-cent per ton payment on 2,000 lbs. of coal, of which only 1,000 lbs. was mined, its depletion allowed is 1,000 × .036, or $36.00, instead of 2,000 × .036, or $72. In other words, its depletion allowance being limited to coal mined, same is not allowed against the payment of $100 made for coal not mined, and same is thereby considered by the Board opinion as a bonus not subject to depletion.

Second. In computing the depletion unit of 3.6 cents, the bonus excluded from its application is given effect, but such effect is disallowed in only allocating the depletion unit against coal mined. This requires some explanation. The respondent's basis for the 3.6 cent allowance is stated in this record (R. 93) as an estimate of 14,000,000 tons of recoverable coal with average mining tonnage of 350,000 tons indicating a mine-life of 40 years with an average annual income therefrom of $34,000. After 40 years, in other words, the entire receivables of petitioner from the instruments amount to $1,360,000, the present worth of which on March 1, 1913, is $510,000. This latter amount divided by 14,000,000 tons gives the unit of 3.6 cents per ton. This method is described in Articles 206 and 211 in petitioner's brief (p. 60). This brings us back to the first proposition as applied to the second. It is that 3.6 cents is based upon the minimum royalties as a factor of computation, but if $34,000 is received annually and only $17,000 of coal is mined, the effect is to allow a depletion only on $17,000, whereby $17,000 is deemed a bonus and is denied depletion. An-

other statement of the situation is that petitioner receives in effect 1.8 cents instead of 3.6 cents per ton upon the $34,000 payment.

Third. The statute with reference to depletion, being a special provision intended to return their capital to the owners of interests in mining properties, the money received for coal paid for involves such return and should be subject to the depletion allowance.

Turning to the schedules in the Board findings we find substantial excess payments under Leases 2 and 4 as follows:

Year	*Mined*	*Paid for*	*Excess*	*Mined*	*Paid for*	*Excess*	*Mined*	*Paid for*	*Excess*
1920...	57,189	120,000	62,811	86,918	100,000	13,082	19.231	187,500	168,269
1921...	54,660	120,000	65,340	15,297	100,000	84,703	25,024	306,250	271,226
1922...	55,864	120,000	64,136	.....	.....	.....	45,483	370,433	324,950
1923...	51,422	120,000	68,578	.....	.....	.....	74,152	340,782	266,630
1924...	57,928	120,000	62,072	.....	.....	.....	103,877	343,657	239,780
1925...	68,804	120,000	51,196	91,170	100,000	8,830	117,792	325,000	207,208
1926...	90,029	120,000	29,971	.....	.....	.....	153,717	335,115	181,408
			404,104			106,615			1,659,471

In these seven years petitioner is deprived of depletion upon 2,000,000 tons—that is, petitioner pays tax upon $72,000, and further analysis serves to increase the amount, although petitioner and respondent agree the decision is wrong and the only Circuit Court of Appeals that has considered the question says the decision is wrong. As we have quoted from *Nichols v. Coolidge, supra*:

"Taxes are very real things."

When respondent and his counsel go into Court in another case to sustain his Departmental position and succeeds, it seems unusual that they should stand precisely for a contrary position herein. The foregoing schedules found relevant by this Court demonstrate the substantial difference between coal paid for and coal mined. It becomes immaterial whether the coal paid for could subsequently be mined because the receipts therefor, considered as a bonus, are subject to depletion, and the rulings of the Board to the contrary have fallen away.

This Court does not in its opinion refer to this point, although petitioners argued same in their brief (pp. 66-70). It is submitted it goes to the very heart of this case and is entitled to consideration. Evidently the *Murphy Oil* decision in the Ninth Circuit is final for respondent has therein sustained his previous position, and has thereby obtained a reduction of the tax for the taxpayer, and both parties are satisfied. It is unfortunate that petitioner and respondent herein were not standing together in this Court against the Board, as they stood at its bar and urged that depletion, if any, was allowable by the statute in this case upon coal paid for. It would be more unfortunate if either party failed to bring the situation to the attention of this Court.

(3) The Court erred in holding the West Virginia judgment is not res adjudicata as to the allowable amount of depletion.

In the Board findings it appears the West Virginia Collector was defended by the United States District Attorney and the General Counsel of respondent. It is a matter of judicial notice that the Collector and Commissioner are each officials of the Government in related capacities as the duties of both are concerned with the collection of the revenue. It is equally clear the Collector was defendant in the West Virginia action, and the Commissioner is the defendant herein, and that neither proceeding is directly against the United States.

In its original brief, petitioner did not argue the United States was the real defendant and respondent laid down the proposition that these appeals were really proceedings against the United States, citing *Sage v. United States.* The situation therefore arises that, admitting a judgment against a Collector is not *res adjudicata* against the United States, whether such judgment is or is not *res adjudicata* against the Commissioner.

This Court does not decide the Commissioner is in effect the United States, and, as apparently the Commissioner and Collector stand in the same relative positions, we do not believe it will so decide. If this is not really a proceeding against the United States, and it is no more so than the proceeding against the Collector, then this Court falls into error in holding *Sage v. United States* is authority for holding the Commissioner is not bound by the judgment against the Collector.

Even though petitioners had maintained that the United States was really the opponent herein and in the West Virginia action, it follows that the *Sage* decision would deny the contention. Thereby the United States was not bound in the West Virginia judgment and was not the real party in interest. Whether the United

States is the real party here remains an undecided question not reached by the *Sage* decision.

This Court, before falling into said error, said:

> "The rule (*res adjudicata*) is applicable, however, only when the subsequent suit is between the same parties or their privies."

and we proceed from this point.

That the Collector and Commissioner were privy in the West Virginia case is found by the Board. The record (p. 89) further recites a consent order signed by the District Attorney and Special Attorney for the Bureau of Internal Revenue as well as the attorneys for plaintiff, and a stipulation of facts and agreement that all papers should be received with the probative weight of testimony from witnesses. Thus the privity in fact is evident if sustained in law.

Here is the case of the respondent Commissioner cooperating with the defendant Collector in defense of the West Virginia action, although not a party of record in same.

In *Beyer Co. v. Fleischmann Co.*, 15 F. (2) 465, (C. C. A., 6), where a similar situation prevailed, we read:

> "The general rule is that one who prosecutes or defends a suit in the name of another, to establish or protect some interest of his own, or who openly assists in an action in aid of some such interest, to the knowledge of the opposing party, is as much bound by the judgment as he would be if he had been a party of record. Penfield *v.* Potts & Co. (6 C. C. A.), 126 F. 475, 61 C. C. A. 351; Greenwich Ins. Co. *v.* Friedman Co. (6 C. C. A.), 142 F. 944, 74 C. C. A. 114; Foote *v.* Parson, etc. (6 C. C. A.), 196 F. 951, 118 C. C. A. 105; Southern Pacific R. Co. *v.* United States, 168 U. S. 1, 18 S. Ct. 18, 42 L. Ed. 355; Souffront *v.* La Compagnie Des Suereries, 217 U. S. 475, 30 S. Ct. 608, 54 L. Ed. 846."

In *White v. Croker*, 13 F. (2) 321 (C. C. A., 5), the rule is again stated:

> "The rule under which one not named in a judgment may be bound thereby in consequence of participation in the suit in which the judgment is rendered is that one who prosecutes or defends a suit in the name of another to protect or establish his own right, or who assists in the prosecution or defense of an action in aid of some interest of his own, and who does this openly to the knowledge of the opposing party, is as much bound by the judgment, and as fully entitled to avail himself of it as an estoppel against an adverse party, as he would be if he had been a party to the record. Souffront *v.* Campagnie, etc., 217 U. S. 475, 30 S. Ct. 608, 54 L. Ed. 846."

In *Souffront v. Campagnie*, 217 U. S. 475, states the same rule:

> "The persons for whose benefit, to the knowledge of the court and of all the parties to the record, litigation is being conducted, cannot, in a legal sense, be said to be strangers to the cause. The case is within the principle that one who prosecutes or defends a suit in the name of another, to establish and protect his own right, or who assists in the prosecution or defense of an action in aid of some interest of his own, and who does this openly, to the knowledge of the opposing party, is as much bound by the judgment, and as fully entitled to avail himself of it, as an estoppel against an adversary party, as he would be if he had been a party to the record. Lovejoy *v.* Murray, 3 Wall. 1, 18 L. Ed. 129."

Further citation seems needless, as it is clear the Commissioner and Collector acted in concert in West Virginia and are equally bound by the result. Privity being admitted, it would reasonably follow the *res adjudicata* of the judgment as to the amount of depletion should be declared by the Court.

(4) The remanding of the Strother appeal is ineffective so far as compliance with the ruling in the Bankers appeal is required, unless said rulings be finally correct.

As the rights of Strother and other stockholders are dependent upon the decision in the case of their corporation, it follows such decision unless complete and correct in all material respects will only increase the error as affecting the stockholders.

If the corporation receipts as proceeds of sales in place effected before the XVI Amendment are not subject to tax, their distribution to stockholders is affected.

If, in the alternative, such receipts are subject to depletion allowances, such allowances must be correct to be properly effective.

If receipts measured by coal paid for but not mined are a bonus, whether same is or is not subject to depletion is material.

These relations between the case of the corporation and the stockholder emphasize the importance of finding the correct answer to the questions raised in these cases.

They demonstrate the propriety of the stockholder joining in this application for rehearing.

In Conclusion.

We respectfully submit as material error the failure of the Court to find:

1. That, as a sale in place is admitted to have taken place before passage of the XVI Amendment, the receipt of proceeds of the certain accrued claim, as paid thereafter, is a return of capital without income capital is to be fully returned before income subject to tax can be ascertained.

2 (*a*) Alternatively, depletion is a special statutory allowance awarded to the owner of an interest in property. Where the interest is terminated by a sale in place,

there can be no remaining interest sufficient to measure a depletion allowance in the proceeds of the sale.

2 (*b*) Alternatively, depletion allowances, if any, exist against all receipts from the depletable interest, including any bonus payment, and in these cases will apply to coal paid for and not merely to coal mined in the several years.

3. Alternatively, depletion allowances, if any, herein as *res adjudicata* through the privity of the Collector and Commissioner in defending the West Virginia action.

We submit the Strother appeal must abide the reconsideration of the opinion in the Bankers case.

We submit any other error, of incidental nature, will disclose itself upon further consideration of the foregoing matters by the Court.

Respectfully submitted,
WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners,
Bankers Pocahontas Coal Co.,
D. J. F. Strother.

Certificate of Counsel.

We, Camden R. McAtee and Wells Goodykoontz, attorneys of record for the petitioners in the above styled cases for review, do hereby certify that the foregoing petition for rehearing is presented in good faith and not for the purposes of delay.

(S.) CAMDEN R. McATEE,
(S.) WELLS GOODYKOONTZ,
Attorneys for Petitioners,
Bankers Pocahontas Coal Co.,
D. J. F. Strother.

PETITION OF RESPONDENT FOR A REHEARING.

Presented February 26, 1932.

(Style of Court and Title Omitted.)

We respectfully request that this Court withdraw the portion of its opinion requiring a rehearing in the Board of Tax Appeals on the grounds:

That this Court is without power to modify or to reverse a decision of the Board of Tax Appeals which is in accordance with law.

The issue in this case was what part of dividends received by petitioner, from the Bankers Pocahontas Coal Company, came out of earnings and what part was a distribution of capital. The income of the Coal Company was composed entirely of royalties received under coal mining leases. The Board found the Company used such part of the royalties as was necessary for administration expenses and to set up a reserve to meet pending Federal taxes, and distributed the balance to the stockholders. (R. 71.) The Company in its appeal (No. 3214) before this Court from the decision of the Board of Tax Appeals in its case, contended first, that the royalties received in the years here in question were part of the sale price of coal in place and constituted a return of capital and not income; or, in the alternative, in case the court should decide against that contention, that it was entitled in computing net income to a deduction for depletion at the rate of 5 cents a ton instead of 3.6 cents as allowed by the Commissioner of Internal Revenue. This Court ruled against the Company in each of those contentions.

It was stipulated by counsel in the present case, that the decision in this case should abide by and follow the decision in the case of the Company upon these two points. The Board of Tax Appeals in its opinion said (R. 45):

To the extent that the distribution made by the corporation constitutes a distribution of its depletion reserve the amount received by Strother is non-taxable. Parties are in full accord as to the treatment to be given the individual appeals.

After the Board's decision herein, each party submitted to the Board proposed recomputations of petitioner's tax liability for the several years in question. After a hearing thereon and after considering the argument of counsel, the Board decided that the proposed redeterminations submitted by respondent were in accordance with its findings of fact and opinion and entered an order in accordance therewith.

On appeal to this Court, petitioner contended that the Board's decision with respect to the part of the distributions in each year that came from depletion, was erroneous. The only basis for this contention is that the proportion of each distribution that should be regarded as depletion, should be the same as the proportion of the Company's receipts that represented depletion. This does not necessarily follow, and the difference may well be accounted for as a result of the application of the method prescribed by Article 1542 of Regulations 45.

However, no facts were shown to prove either that the Commissioner's computations were incorrect under Article 1542, or if incorrect that the figures presented by petitioner are right. The burden was upon petitioner to show what the correct tax should be. See *Reinecke* v. *Spalding*, 280 U. S. 227.

This Court held that the Board should give further consideration to the case and afford the taxpayer an opportunity to introduce additional testimony to bring out facts necessary to a decision of the issues involved, and it remanded the case for further proceedings.

It is believed that no question of law was presented to this Court, and that the issues raised by petitioner could not have been passed upon by this Court because of an absence of facts to raise those issues. In these circumstances, it does not appear that there was any error of law in the Board's decision and this Court is therefore without power to remand the case for further hearing.

A petition for rehearing upon this ground in a similar situation was recently presented and is now pending in this Court in the case of *H. A. Underwood v. Commissioner*, No. 3208, decided January 12, 1932. The argument there presented in favor of the relief asked for by respondent is applicable with equal force to the present case. To avoid repetition, reference is made to that petition and that argument is incorporated herein by reference.

Conclusion.

We respectfully submit that the portion of the opinion requiring a rehearing in this case by the Board of Tax Appeals should be withdrawn. If the Court is not convinced that this should be done, we respectfully request that the case should be set down for rehearing in this Court in order that we may have further opportunity to present our views.

G. A. YOUNGQUIST,
Assistant Attorney General.

J. LOUIS MONARCH,
ANDREW D. SHARPE,
Special Assistants to the Attorney General.

February, 1932.

Certificate of Counsel.

The undersigned, counsel for respondent, the Commissioner of Internal Revenue, hereby certifies that in his judgment, the foregoing petition is well founded and is not interposed for delay.

G. A. YOUNGQUIST,
Assistant Attorney General.

ORDER DENYING REHEARINGS.

Filed and Entered March 7, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS.
FOURTH CIRCUIT.

No. 3214.

D. J. F. Strother, Petitioner,

versus

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

THIS COURT having at its January term, 1932, rendered its decision remanding this cause to the said United States Board of Tax Appeals for further proceedings in accordance with the opinion of this Court in case No. 3215, *Bankers Pocahontas Coal Company versus Commissioner of Internal Revenue*, in so far as it determines the questions involved herein, and without prejudice to the right of petitioner to rely upon the legal positions as to others matters urged upon this appeal, in accordance with the opinion of the Court filed herein, and the petitioner having on February 26, 1932, presented to the Court a petition for a rehearing of the said cause, and the respondent having on February 26, 1932, presented to the Court a petition for a rehearing of the said cause, and the said petitions for rehearing having been carefully considered,

IT IS NOW HERE ORDERED by this Court that the rehearings asked for, be, and the same are hereby, denied. Let mandate issue after the expiration of five days from this date.

JOHN J. PARKER,
Senior Circuit Judge.

March 7, 1932.

March 11, 1932, petition of petitioner for a stay of the mandate is filed.

Same day, order staying the mandate is filed.

MOTION FOR LEAVE TO FILE SUPPLEMENTAL PETITION FOR REHEARING AND REARGUMENT.

Filed in Open Court April 12, 1932.

(Style of Court and Title Omitted.)

Come now petitioners in the above entitled proceeding, by their attorneys, and tender their supplemental petition for rehearing and reargument, and move the Court for leave to file same, and to fix a date for hearing the parties on same.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

SUPPLEMENTAL PETITION OF PETITIONER FOR REHEARING.

Filed by leave granted in Open Court April 12, 1932.

(Style of Court and Title Omitted.)

By leave of Court therefor asked and granted: Petitioners respectfully request—

(1) A reconsideration of the denial of the Petition for Rehearing heretofore filed on February 26, 1932.

(2) Opportunity by oral argument to present reasons for said rehearing.

For cause:

(*a*) Court Rule 29, providing a petition for rehearing "will not be granted, or permitted to be argued, unless a judge who concurred in the judgment desires it and a majority of the Court so determined", was construed by counsel to intend that the Court, as constituted at the hearing would *en banc* consider such petition. Accordingly, it was the impression the Court would not so sit together until April, 1932, at Richmond, Virginia. Consequently, no request for oral hearing upon the petition, and no brief in elaboration of reasons therefor was believed to be required until the Court would sit in April, 1932.

(*b*) Only after decision of these cases on January 25, 1932, did the petitioners and attorneys receive the opinion for their consideration.

On February 8, 1932, stay of the mandate was ordered on condition that within 30 days petition for rehearing

be filed or application be made for certiorari to the Supreme Court. Petitions for rehearing were duly filed by both parties, and were denied on March 7, 1932, with direction for issue of mandate after five days.

On March 11, 1932, this Court ordered a stay of mandate for 60 days pending application for certiorari. (* * * "unless otherwise ordered by this or the Supreme Court, and provided said application is filed in said Supreme Court within 60 days from this date.")

Thus, between the date of decision on January 25th and denial of rehearing on March 7, 1932, within 42 days, the petition for rehearing and its denial occurred, at a time of year and under present business conditions when the Court and counsel and litigants were necessarily engaged in giving attention and time to other important affairs of public and private character.

(*c*) As the right to change the order for stay of the mandate (quoted above) is reserved, the propriety of a rehearing is still believed to rest in and with the Court and may properly be granted if good and sufficient ground is shown therefor.

(*d*) This Court was created and constituted as a relief tribunal to the Supreme Court and strives to relieve that other great Court of the heavy labor imposed upon it, unless and until it feels bound as to finality of disposition of causes before it, when subsequent holdings after presentation of cases may and do occasion as here further consideration of fact or law.

(*e*) This decision and opinion are based on rules of law herein not pertinent to the facts, particularly in holding rules of taxation as to income of mines and their products determine the case when only real estate and its sale, *and not mines and their products,* is the subject matter presented herein. Verbal explanation is essential to

presentation of a due understanding of the facts and to show the methods of income determination approved herein as applicable to the facts of these cases find no justification in the Revenue Acts.

(*f*) That the points made against the decision and opinion in the petitioners' Petition for Rehearing and their briefs, especially their Reply Brief, upon oral presentation of their soundness, will demonstrate the propriety of a holding contrary to the pronounced decision.

(*g*) That the decision of these cases according to law upon the rights involved presents or creates no precedent in taxation, as their facts indicate their concern with a deplorable coal land condition pointing to future decreases of the purchase money payments derived from sales made before the effective date of the XVI Amendment.

(*h*) That the orders of the Court as to further disposition of the cases entail further delay to that now accrued in disposing of them. Congress may not impose excessive fines (Article VIII, Constitution), yet herein large levies against capital assets, which are not income or profits accrued after 1913, have been required and satisfied, and carry additional penalties while the power so to tax said assets is in litigation these past twelve years.

This attrition through tax and penalty and incidental expense, merely because taxpayers are legally and by due process contesting the rights asserted against them, demonstrates the power to tax is the power to destroy and that industry will languish under the oppression of taxes levied in the name of progress.

(*i*) The denial of certiorari by the Supreme Court in any case, wherein the findings appear to modify or con-

tradict previous decisions of the Supreme Court does not establish nor approve such modification or contradiction. In *Atlantic C. L. Co. v. Powe,* 283 U. S. 401, 75 L. Ed. 1142, answering this precise question the Court quoted from its opinion in *United States v. Carver,* 260 U. S. 482, 67 L. Ed. 361, wherein it decided:

> "The denial of a writ of certiorari imports no expression of opinion upon the merits of the case, as the bar has been told many times. Therefore it is unnecessary to consider whether the libellants' argument is supported by the decisions to which they refer."

(*j*) The *briefs* filed by the litigant parties did not refer to, nor did the *opinion* of this Court cite certain Federal Court decisions *reported* since the date of the decision. Evidently neither the Court nor counsel had those decisions before them at or before the decision or the order denying rehearing; said decisions are:

Commissioner v. Brown, 54 F. (2) 563 (Federal Reporter Feb. 22, 1932).

Old Colony Railroad Co. v. Commissioner, U. S. Supreme Court Advance Ops. No. 7, 1931 Term, p. 317; 76 L. Ed. 317.

Crile v. Commissioner, 55 Fed. (2) 804 (Federal Reporter April 4, 1932).

Hernandez, Collector, v. Becker, 54 F. (2) 542. (Federal Reporter Feb. 22, 1932).

Harmel v. Commissioner, — Fed. (2) —, (Federal Reporter, — 1932).

Second National Bank v. Woodworth, 54 F. (2) 672 (Federal Reporter February 22, 1932).

Murphy Oil Co., v. Commissioner, 55 F. (2) 17 (Federal Reporter, March 21, 1932).

Brief reference is here made to these recent decisions:

Petitioners contend that before the incidence of the XVI Amendment they owned the right to receive the purchase money contracted to be paid by the purchasers of coal sold to said purchasers in 1902, upon the basis of the coal thereafter taken out of the stratum or coal seam, and the liability of petitioners to income tax upon such contract receipts is the controversial subject. The claim to said receipts, *if an unconditional obligation* existing on and before passage of the XVI Amendment, when subsequently collected, does not constitute taxable income, this being the general rule. In *Commissioner v. Brown,* 54 F. (2) 563 (C. C. A.-1), such a claim, *existing as a conditional obligation,* is held not to be income when subsequently collected, upon authority of *Burnet v. Logan,* 283 U. S. 404. These decisions read together, or separately, are an all sufficient solution of the present cases.

Petitioners contend that, having prior to the XVI Amendment and Revenue Acts made contracts and thereby sold realty and passed the title to same, the subsequent payments do not constitute taxable income, and *Old Colony Railroad Co., v. Commissioner,* U. S. Supreme Court Adv. Op. 7, 1931 Term, 317, supports this position. The second, third, fourth and fifth head-notes of that decision are:

> Second. "Premiums received on corporate bonds issued *prior* to the effective date of the Sixteenth Amendment to the Federal Constitution, authorizing Federal taxation of incomes, *may not* be made the *basis* of subsequent income taxation, although the Interstate Commerce Commission has required them to be amortized over the period of the respective lives of the bonds and a yearly ratable proportion thereof to be reported as income."

Third. "The amount of interest on bonded indebtedness which may be deducted from gross income in determining taxable income is the amount *contracted to be paid,* notwithstanding the fact that as the bonds were issued at a premium, the effective rate is less."

Fourth. "The legislature must be presumed to use words in their known and ordinary significance; and this rule is applicable to taxing acts."

Fifth. "Terms used in tax statutes are, in case of *doubt,* to be given the construction *most favorable* to the taxpayer."

Mr. Justice Roberts' reasoning in the opinion squares with the holdings referred to in the above cited cases and means that when payments are received or *contracted* to be received before taxing acts come into being, those payments can not be made a proper *basis* of *taxation* by subsequent legislation.

Petitioners contend the contract payments collected in the taxable years are not subject to tax as the realization of obligations created and existing before the XVI Amendment. In *Crile v. Commissioner,* 55 Fed. (2) 804, (C. C. A.-6), a sum of money was paid to taxpayer as part consideration of a lease and the Court says:

"Where, there is an intent to create in the 'lessee' an interest in the property itself—as by way of purchase,—even though that interest may be forfeitable by failure to perform conditions subsequent, and this intent is made manifest by the instruments duly executed to carry it into effect, the attending payment is a return of capital, and should be so regarded, at least prior to forfeiture and reversion."

Therefore, as there was here an admitted sale, the pay-

ment of purchase money is a return of capital. As the vendor is without further interest in the property neither he nor his assigns can claim depreciation or depletion as to the property conveyed.

Petitioners raised the point that for all purposes, including purposes of taxation, the statutes and rules of property in a state were controlling in the Federal Courts. This Court's decision and opinion discounts this contention, yet in *Hernandez, Collector v. Becker,* 54 F. (2d) 544, dealing with a federal estate tax, Judge Phillips held the character of the estate from which the federal tax came was controlled by the statutes and rules of property of the state.

In *Harmel v. Commissioner,* Fed. (2) (C. C. A.-5), the rule that an oil and gas lease conveys a determinable fee to minerals in place under the Texas laws and rules of property is expressly upheld, and the special capital gain provision instead of the general tax upon ordinary income, as provided in the Revenue Acts, is held to measure the income tax liability upon the resulting gain to the taxpayer.

Petitioners raised the point that the Collector and the Commissioners were in privity and a judgment against one was binding against the other. This Court discredited that position, yet *Second National Bank v. Woodworth,* 54 F. (2) 672 (Judge Simons) holds a collector of internal revenue is agent or trustee for the government and refers to and discusses at length Mr. Justice Holmes' decision in the *Sage* case, relied on in the opinion (250 U. S. 33), and his remarks are applicable to the instant cases:

> "There is an important distinction between the facts of the case at bar and those of the *Sage* case."

The distinction in the *Woodworth* case is that the judgment put forward in bar by the Collector is one against

the United States, whereas in the *Sage* case the judgment so put forward by the United States was against the Collector. In the *Woodworth* case, the judgment in bar is held sufficient on the ground that, as the suit is against the Collector by reason of his official acts as a public officer and official agent or trustee of the Government, therefore:

> "It may be conceded that a judgment against an agent does not bind the principal, but that is not to say that the converse is true, and that a judgment against the principal is not a bar against the agent, where the latter is privy with the former in respect to the subject matter of the suit."

Judge Simon, after suggesting the argument of Mr. Justice Holmes is *dicta,* rests his decision not directly upon *Sage v. United States,* but upon *Bank of Kentucky v. Stone,* 174 U. S. 799, 43 L. Ed. 1187, wherein a judgment enjoining a town from enforcing a tax was held to bar a similar proceeding against its board of assessors.

In these present cases, the judgment is against the Collector, the agent and not the principal, the United States. That a judgment against its officer is not conclusive upon the United States has long been settled on the basic grounds that the Government cannot be sued without its consent that its officers may not waive this immunity, and that the Government cannot be compelled into Court to litigate with private parties in defense of its property, as decided in *Carr v. United States,* 98 U. S. 433, 25 L. Ed. 209. But that its officer may be sued and that its other officer in privity in the matter and aiding in defending the proceeding may be, and is, bound by the ensuing judgment, is not to say that the Government is likewise bound. But saying the Government is not bound is no justification for concluding its other of-

ficer is not bound. Thus, in *Johnson v. Herold*, 161 Fed. 593, 602, sixteen actions for recovery of identical taxes were brought against various collectors by the plaintiff, and a judgment in one case was held conclusive in the others, thus binding plaintiff or the collector not a party to the decided cause.

Without further quotation from the *Woodworth* opinion, attention is invited to the analysis of the *Sage* case in this most recent, well considered opinion, particularly the last paragraph and it would seem clear that by reason and decision of the very highest court there is privity which should be recognized between *White, Collector,* and the *Commissioner of Internal Revenue* over the same subject matter—both are agents and trustees for the United States. In one case the tax illegally collected is returned, and in these cases the Commissioner is endeavoring to collect another illegally imposed tax. Both acts are by the agents and trustees of the principal. The agents are not personally liable. The right and reason of the *Woodworth* case is apparent.

Petitioners contend, if depletion is computable as an allowable deduction herein, same should be upon the basis of coal paid for and not of coal mined, pointing out that respondent took the same position before the Board. The Petition for Rehearing (pp. 22-26) discusses this issue, with some reference to *Murphy Oil Co. v. Burnet*, 55 F. (2) 17 (C. C. A.-9), wherein on January 11, 1932, the Board's position was held erroneous that payments for coal not mined constituted bonuses not subject to depletion allowances. This ruling was obtained by petition for review filed by respondent.

Judge Wilbur justifies this ruling first on the facts of the *Murphy* case, and then upon the development of the depletion principle as developed in statute, decision and regulation, and utterly destroys the Board concept which this Court has approved in its affirmance of the Board. He concludes:

> "The statute, with reference to depletion * * * is a special one * * * involving the production of oil and minerals from mines, and the consequent *return of capital by the owers of interests therein,* and controls over other general provisions of the law in regard to the return of capital investment." (Our italics.)

But, as decided above, a sale of mineral in place in Texas creates a determinable fee in the purchaser and the profit is taxable as a capital gain. As this Court has likewise decided, a sale of mineral in place in West Virginia was effected herein in 1902. As said in the *Crile* decision, *supra,* the creation of an interest in the "lessee" made the consideration a return of capital. It follows petitioners are not the owners of any interests in the mines or coal, and cannot avail themselves of depletion allowances, nor have same forced upon them.

In Conclusion.

This application is lengthy and yet incomplete, and full understanding of the facts and law depend upon verbal presentation and discussion of their aspects that the simple truth may appear. But the present and future stress of the taxpayers make such application imperative, and, with due apology that no imposition upon the time or patience of the Court or its members is intended, still these requests are made:

1. That this petition and application be permitted to be filed.

2. That opportunity be granted the parties to appear at an early date and orally present argument as to the propriety of a rehearing.

3. That upon rehearing the petitioners be declared not liable for income and profits taxes upon the contract proceeds from the sales of coal in place effected before the XVI Amendment.

Respectfully submitted,

D. J. F. STROTHER,
BANKERS POCAHONTAS
COAL CO.,
Petitioners.
By WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys.

Certificate of Counsel.

We, Wells Goodykoontz and Camden R. McAtee, attorneys of record for the petitioners in the above styled cases for review, do hereby certify that the foregoing petition for rehearing is presented in good faith and not for the purposes of delay.

(S.) WELLS GOODYKOONTZ,
(S.) CAMDEN R. McATEE,
Attorneys for Petitioners,
Bankers Pocahontas Coal Co.,
D. J. F. Strother.

ORDER DENYING REHEARING AND STAYING MANDATE.

Filed and Entered April 29, 1932.

UNITED STATES CIRCUIT COURT OF APPEALS

Fourth Circuit.

No. 3214.

D. J. F. Strother, Petitioner,

vs.

Commissioner of Internal Revenue, Respondent.

On Petition to Review the Decision of the United States Board of Tax Appeals.

ON CONSIDERATION of the supplemental petition of the pteitioner for a rehearing of the above entitled cause, filed by leave of Court on April 12, 1932,

IT IS NOW HERE ORDERED by this Court that the rehearing asked for in the supplemental petition be, and the same is hereby, denied.

IT IS FURTHER ORDERED that the mandate of this Court in this cause be, and the same is hereby, stayed pending the application of the petitioner in the Supreme Court of the United States for a writ of certiorari to this Court, unless otherwise ordered by this or the said Supreme Court, and provided said application is presented in the said Supreme Court on or before May 23, 1932.

JOHN J. PARKER,
Senior Circuit Judge.

CLERK'S CERTIFICATE.

UNITED STATES OF AMERICA,
Fourth Circuit, ss:

I, CLAUDE M. DEAN, Clerk of the United States Circuit Court of Appeals for the Fourth Circuit, do certify that the foregoing is a true copy of the record and proceedings in the therein entitled cause, as the same remain among the records and files of the said Circuit Court of Appeals.

IN TESTIMONY WHEREOF, I hereto set my hand and affix the seal of the said United States Circuit Court of Appeals for the Fourth Circuit, at Richmond, Virginia, this 7th day of May, A. D. 1932.

(Seal of Court)

CLAUDE M. DEAN, Clerk,
U. S. Circuit Court of Appeals,
Fourth Circuit.

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed October 10, 1932

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Fourth Circuit is granted, and the case is assigned for argument immediately following case No. 80, Murphy Oil Co. vs. Burnet, Commissioner of Internal Revenue.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

FILE COPY

Office Supreme Court, U. S.
FILED
MAY 23 1932
CHARLES ELMORE CROPLEY
CLERK

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1931.

No. ~~282~~ 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE.

No. ~~288~~ 105

D. J. F. STROTHER, PETITIONER,

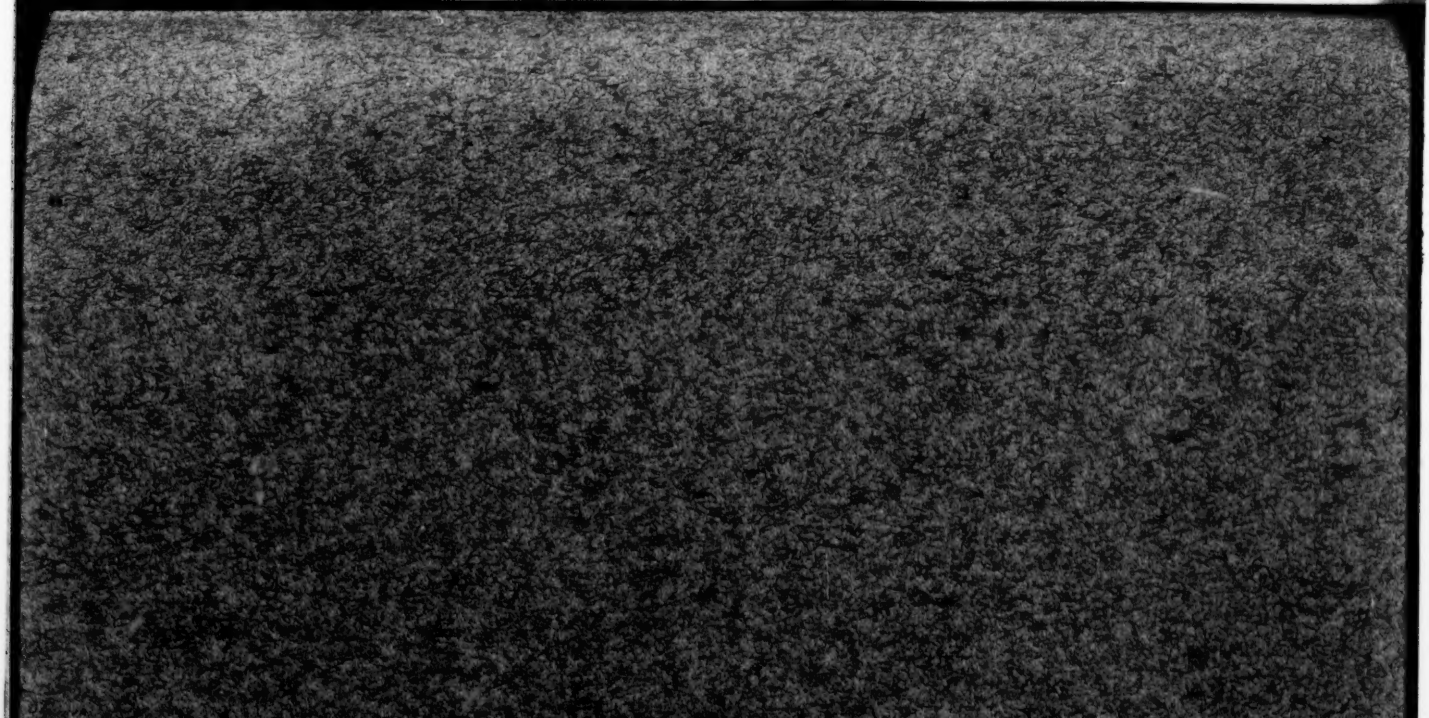
v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

MASON, SPALDING & McATEE,
GOODYKOONTZ AND SLAVEN,
Of Counsel.



INDEX.

Subject Index.

	Page
Petition for writ	1
Judgments below	1
Questions presented	2
Constitution, statutes, and regulations	4
Statement	4
Specifications of error	8
Reasons relied on for allowance	10
Prayer for writ	10
Brief in support of petition	13
Opinions below	13
Jurisdiction	13
Statement of case	14
Reasons for review and specification of errors	14
Argument	14
Conclusion	35

Decisions Cited.

Alexander v. King, 46 F. (2) 235	22
Atlantic C. L. Co. v. Powe, 283 U. S. 401	23
Bank of Kentucky v. Stone, 174 U. S. 799	33
Berg v. Commissioner, 33 F. (2) 641	24
Beyer v. Fleishmann Co., 15 F. (2) 465 (C. C. A.-6)	34
Blair v. Oesterlein M. Co., 27 U. S. 220	31
Bromley v. McCaughn, 280 U. S. 124	25
Brushaber v. Union P. R. Co., 240 U. S. 1, 18	16
Burnet v. Coronado Oil and Gas Co., — U. S. — (April 11, 1932)	20, 22
Burnet v. Logan, 283 U. S. 404	19
Burnet v. Thompson Oil & Gas Co., 283 U. S. 301	21
Carr v. United States, 98 U. S. 433	31
Crile v. Commissioner, 55 F. (2) 804 (C. C. A.-6)	18
Crooks v. Harrelon, 282 U. S. 55	25
Darby Lynde Co. v. Commissioner, 51 F. (2) 32	21
Evans v. Gore, 253 U. S. 245	16
Ferguson v. Commissioner, 45 F. (2) 573	22
Greylock Mills v. White, 55 F. (2) 704	33

	Page
Group No. One Oil Corp. v. Bass, 283 U. S. 279	20, 22, 25
Harmel v. Commissioner, — F. (2) — (C. C. A.-5)	22
Hirschi v. United States, 67 Ct. Cl. 637	23
Jefferson Gas Coal Co. v. Commissioner, 52 F. (2) 120 (C. C. A.-3)	20
Kaufman's Case, 96 U. S. 568	32
McCormick v. Sullivant, 10 Wheat. 192	25
Minnesota v. Hitchcock, 185 U. S. 373	34
Murphy Oil Co. v. Burnet, 55 F. (2) 17 (C. C. A.-9)	27
Nichols v. Coolidge, 274 U. S. 531	19
Old Colony Trust Co. v. Commissioner, 279 U. S. 716	31
Old Colony R. R. Co. v. Commissioner, 279 U. S. 716, 727 (52 S. Ct. 211)	14, 17
Park v. Gilligan, 293 Fed. 129	16, 18
Phillips v. Commissioner, 283 U. S. 589	25
Poe, Collector, v. Seaborn, 282 U. S. 101	24, 25
Pollock v. Farmers L. & T. Co., 157 U. S. 429	16
Pugh v. Commissioner, 49 F. (2) 76 (C. C. A.-5)	21
Rosenberger v. McCaughn, 25 F. (2) 699 (C. C. A.-5)	24
Sage v. United States, 250 U. S. 33	29
Sanders v. Commissioner, 29 F. (2) 832 (C. C. A-5)	16
Schneider v. Duffy, 43 F. (2) 642	17
Scranton v. Wheeler, 179 U. S. 141	32
Second National Bank v. Woodworth, 54 F. (2) 672	33
Souffront v. Compagnie, 217 U. S. 475	35
South Vernon Oil Co. v. Hopkins, 49 F. (2) 1028 (C. C. A.-5)	21
Stanton v. Baltic Mining Co., 240 U. S. 103	16, 21
Steedman v. United States, 63 Ct. Cl. 226	25
Stratton's Independence v. Howbert, 231 U. S. 399	17
Trudal v. Wesley, 167 U. S. 204	32
Tyler v. United States, 281 U. S. 497	25
United States v. Carver, 260 U. S. 482	23
United States v. Fox, 4 Otto 315	25
United States v. Frerichs, 124 U. S. 315	32
United States v. Guinzberg, 278 F. 363 (C. C. A.-3)	16
United States v. Lee, 106 U. S. 196	31, 32
Weiss v. Wiener, 279 U. S. 533	1/
Wells v. Nickles, 104 U. S. 444	32

CONSTITUTION AND STATUTES CITED.

Constitution, Amendment XVI	5, 14, 15, 16, 19, 36, 37

Individual Gross Income.

	Page
R. A. 1918, Section 213 (40 St. L. 1057-96, C. 18)	37
R. A 1921, Section 213 (42 St. L. 227, C. 136)	37
R. A. 1924, Section 213 (43 St. L. C. 234)	37
R. A. 1926, Section 213 (44 St. L. (Part 2) 9, C. 27)	38

Individual Net Income.

R. A. 1918, Section 212 (Idem as above)	38
R. A. 1921, Section 212	38
R. A. 1924, Section 212	38
R. A. 1926, Section 212	38

Corporation Gross Income.

R. A. 1918, Section 233 (Idem as above)	38
R. A. 1921, Section 233	38
R. A. 1924, Section 233	38
R. A. 1926, Section 233	39

Corporation Net Income.

R. A. 1918, Section 232 (Idem as above)	39
R. A. 1921, Section 232	39
R. A. 1924, Section 232	39
R. A. 1926, Section 232	39

Meaning of Net Income.

Article 21 (Reg. 45, 62, 65, 69)	39
Article 531 (Reg. 45, 62, 65, 69)	41

Income Accrued Prior to March 1, 1913.

Article 90 (Same)	41

Corporation Deductions (Depletion).

R. A. 1918, Section 234 (Idem as above)	42
R. A. 1921, Section 234	42
R. A. 1924, Section 234	43
R. A. 1926, Section 234	43

Returnable to Lessor.

Article 204 (Same)	43

Adjustments as to Bonus.

Page
Article 215 (Reg. 45, 62, 65) 44
Article 216 (Reg. 69) 44

Dividends.

R. A. 1918, Section 201 (Idem as above) 45
R. A. 1921, Section 201 46
R. A. 1924, Section 201 47
R. A. 1926, Section 201 47

Sources of Distribution.

Article 1542 (Same) 47
Article 1543 (Same) 47

Distribution from Depletion Reserves.

Article 1546 (Same) 48

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1931.

No.

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE.

No.

D. J. F. STROTHER, PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR WRITS OF CERTIORARI.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Above petitioners respectfully petition that writs of certiorari issue herein for cause as follows:

The Judgments Below.

For review of the judgments of the United States Circuit Court of Appeals for the Fourth Circuit en-

tered respectively in causes, *No. 3214, D. J. F. Strother* v. *Commissioner of Internal Revenue,* and *No. 3215, Bankers Pocahontas Coal Company* v. *Commissioner of Internal Revenue,* in said Court, (*said cases being previously heard together*), on January 27, 1932 (Record, page 135) (Opinion on January 25, 1932) (Record, pp. 119-132) (55 F. (2) 626), affirming (and reversing in parts not here important), the decision of the United States Board of Tax Appeals (Record, page 71) (Findings and opinion on January 22, 1930, Record, pp. 37-57) (18 B. T. A. 901), that deficiencies in income and profits tax for the years 1920 to 1926 in the amount of $39,171.05 were owing by petitioner company, and deficiencies in income taxes of $5,806.11 were owing by petitioner Strother.

(Certified copies of the record in each case, showing the pleadings, findings and opinion of the Board, petition for review, statement of evidence, proceedings and opinion of the Court of Appeals, accompany this petition.)

Questions Presented.

The proceedings involve the alleged liability of petitioner company for income and profits taxes for the years 1920 to 1926, inclusive, and of its stockholder, petitioner Strother, for income taxes for the years 1919 to 1926, inclusive, as determined against petitioners by the Commissioner of Internal Revenue, the substantial questions being:

1(*a*). Whether the purchase money proceeds of sales of coal in place effected in 1902 and pay-

able by the grantees in subsequent years in determinable amounts without interest as installments of said purchase money, are taxable income when collected in the years in controversy by petitioner company, who, at, before and after March 1, 1913, always owned the unconditional claim then existing to recover or receive the unpaid part of said purchase money in the several subsequent years, and did thereafter collect same.

1(*b*). Whether the distribution of said purchase money proceeds to the stockholder Strother constitutes taxable income to him in said years.

2. Whether Congress intended by the Revenue Acts to tax said proceeds of sale, and if so—

2(*a*). Whether the grantor of coal sold in place is a lessor, and as such entitled to the statutory depletion allowances of a lessor, and if so—

2(*b*). Whether the excess amount of minimum payments received in any year from the grantee over the payment thereby made for coal actually mined within the year is not subject to any depletion allowance.

3. Whether a judgment against a Collector, who was therein defended of record by the Commissioner of Internal Revenue, and which judgment involves the same subject matter of reason-

able depletion as is presented herein, and was duly paid by the United States, is *res adjudicata* against the Commissioner as to the amount of depletion, if any, allowable to petitioner company.

The Circuit Court of Appeals affirmatively answered each question except question 3, which was negatively answered, and petitioners would show its resulting decision is thereby in conflict with the weight of authority and decision upon these legal questions which affect many taxpayers.

Constitution, Statutes and Regulations Involved.

Same are contained in the Appendix to the supporting Brief.

Statement.

In 1901 and 1902, certain predecessors in title of petitioner company, as fee owners of West Virginia coal lands, valueless except for their coal content (R. p. 39), demised the coal in place to various operators for a fixed price payable upon the basis of each ton of coal mined by the operator in each year thereafter, with a fixed lump sum as the minimum annual payment regardless of whether coal representing that amount was mined within the year (R. pp. 40-41). The operators and their successors have always since possessed the acreage and mined the coal therefrom (R. p. 39). Said demise under the laws of West Virginia effected a sale of coal in place (R. p. 49; p. 123, Opinion of the lower Court).

In 1912, petitioner company acquired the fee title to said acreage subject to said previous sales of coal in place, and also acquired all the rights of its predecessors in title to collect the considerations payable by the operators, and has always since collected same when paid in the subsequent years, receiving thereby the proceeds of the minimum payments as well as any payments for coal actually mined each year (R. p. 39). Petitioner company, upon a cash basis (R. p. 46) each year distributed all its receipts to its stockholders, excepting amounts retained for payment, if necessary, of the taxes here in controversy (R. p. 72).

After adoption of the XVI Amendment and passage of the Revenue Acts, both petitioners in their tax returns disclosed said payments as being the proceeds of sales of coal in place effected before the Amendment, and consequently not subject to tax (R. pp. 38, 46, 49). However, the Commissioner of Internal Revenue for the years 1914-1919 held petitioner company and the operators were lessor and lessees, and said payments were gross income, including a capital return, and subject to a depletion allowance of 3.6 cents per ton of coal mined, to eliminate the capital return. The Commissioner thereupon assessed and required petitioner company thereby to pay taxes of about $6,000 to the proper Collector upon the alleged net income so ascertained (R. p. 47). Petitioner company, thereupon, sued said Collector in the United States District Court in West Virginia to recover said taxes for cause, either, that same were not taxable, being the proceeds of purchase money contracted for before the XVI

Amendment, existing unconditionally on March 1, 1913, and payable thereafter, or alternatively, if petitioner company was a lessor and not a vendor, that the depletion unit allowable to return the capital should be fixed in a greater amount (R. p. 47). At the trial of said action, in which the Commissioner of Internal Revenue by his counsel was defending the Collector, petitioner company obtained a final judgment fixing a depletion unit of 5 cents per ton, and a consequent recovery of a substantial part of the taxes, which judgment was duly satisfied and has since remained in full effect (R. p. 47).

Contemporaneous with and subsequent to said litigation, said Commissioner determined and assessed petitioner company with income taxes of about $40,000 (R. p. 38) for the years 1920-1926, holding petitioner was a lessor, allowing a depletion of 3.6 cents per ton, and refusing to give effect to the 5 cent depletion rate established by said judgment (R. pp. 46, 47, 48).

As to petitioner Strother, the Commissioner increased his net income for the several years by his entire receipts from said purchase money distributions, without any allowance for depletion reserves so received, and determined the resulting deficiencies of tax against him.

Petitioners, by their appropriate appeals, petitioned the United States Board of Tax Appeals for redeterminations of said several deficiencies, claiming petitioner company was neither the owner nor lessor of any mine, and the alleged income was not taxable to either petitioner, since same represented purchase

money payments upon sales of coal in place effected before March 1, 1913, and payable thereafter without income increment, and claiming—in the alternative—that if the alleged income was taxable after allowance of depletion deductions, the 5 cent depletion rate established in previous litigation between the parties was *res adjudicata* thereof, and should be allowed instead of the 3.6 cent rate (R. pp. 7, 8, 18, 19). The Board of Tax Appeals, without denying that the demise of 1902 effected a sale of coal in place according to the property rule of West Virginia (R. p. 49), held: *First,* the contracts for federal tax purposes established the relation of lessor and lessee between petitioner company and the operator, making thte payments gross income subject to depletion allowances (R. p. 50); *Second,* that bonuses, or minimum payments in excess of payment of coal actually mined in the year, are gross income not subject to depletion allowances (R. pp. 49, 70); and *Third,* the depletion rate of 5 cents per ton determined in previous litigation between the parties over the same subject matter was not thereby allowable to petitioner company (R. p. 52), and said Board determined total deficiencies of $39,171.05 against petitioner company (R. p. 71), and thereby of $5,806.11 against petitioner Strother.

By their petitions for review (R. p. 73) petitioners applied to the Circuit Court of Appeals for the Fourth Circuit for review of said Board decision, alleging as errors: (1) That such payments were not taxable income (R. p. 81); (2) Alternatively, that the adjudged 5 cent depletion rate was applicable (R. p. 81); and (3)

That any depletion was allowable upon coal paid for and not merely upon coal mined (R. p. 82); and, (4) As to petitioner Strother, that he received no taxable income, or if so, that he was entitled to elimination of depletion reserves distributed to him.

The Circuit Court of Appeals held, *First,* the contracts of 1902 effected sales of coal in place (R. p. 123); *Second,* that, nevertheless, Congress intended to tax said sales proceeds by returning capital through lessor depletion allowances (R. p. 124); *Third,* that the West Virginia judgment was not binding upon the Commissioner and hence did not establish the 5 cent depletion rate (R. p. 127); and *Fourth,* affirmed the Board determination whereby the minimum annual payments in excess of payment for coal actually mined were held to be bonuses returnable as gross income without allowance of depletion deductions against same (R. 132). It further held the Strother case was substantially to be determined by its decision of the company case (R. p. 132). Incidental issues not here of importance are omitted as immaterial.

Original and supplemental applications for rehearing (R. pp. 137, 171) were denied by the Court (R. pp. 169, 185) and its mandate has been stayed pending the filing of this application for certiorari (R. 185) in proper time.

Specifications of Error.

The Board and Court below erred (references to opinion of each):

1. In deciding that the purchase money proceeds of sales of coal in place effected in 1902 and payable by

the grantees in subsequent years in determinable amounts without interest as installments of said purchase money, are taxable income to petitioner company who, at and before March 1, 1913, owned the unconditional claim then existing to recover or receive the unpaid part of said purchase money in the several subsequent years, and did thereafter collect same (R. pp. 49, 124).

1(*b*). In deciding that the distribution of said proceeds to the stockholder Strother is taxable income to him (R. pp. 57, 135).

2. In deciding that Congress intended by the Revenue Acts to tax said proceeds of sale (R. p. 124.)

3. In deciding that the grantor of coal sold in place is a lessor, and as such entitled to the statutory depletion allowances of a lessor (R. pp. 51, 124).

4. In deciding that the excess amount of minimum payment received in any year from the grantee over the payment thereby made for coal actually mined within the year is not subject to any depletion allowance (R. pp. 49, 134).

5. In deciding that the judgment against a Collector, who was therein defended of record by the Commissioner of Internal Revenue, and which judgment involves the same subject matter of reasonable depletion as is presented herein, and was duly paid by the United States, is not *res adjudicata* against the Commissioner

as to the amount of depletion, if any, allowable to petitioner (R. pp. 52, 127).

Reasons Relied On for Allowing the Writ.

1. The Circuit Court of Appeals has rendered herein a decision contrary to the XVI Amendment, and in conflict with decisions of this Supreme Court of the United States and of other Circuit Courts of Appeals on the same subject matter.

2. The Circuit Court of Appeals has decided an important question of Federal taxation in a way in conflict with a decision of another Circuit Court of Appeals; it has further decided an important question of *res adjudicata* in a way probably untenable and which should be settled by this Court.

3. The present case involves questions of general interest, affecting not alone the tax liability of petitioners, but that of many other taxpayers as well, involving basic issues as to taxable or non-taxable income, the power to levy income taxes under the XVI Amendment, and the effect of prior litigation upon the rights of parties, on which matters an authoritative ruling of this Court is of public importance, and is respectfully requested herein.

There is presented herewith a supporting brief, showing more fully petitioner's views on the questions involved.

WHEREFORE, the premises considered, your petitioners respectfully pray for issue of writs of cer-

tiorari to review the judgments of the Circuit Court of Appeals for the Fourth Circuit in the aforesaid cases of petitioners, and for entry of all proper orders thereto required and necessary, and for all such other and further relief as may seem meet and just.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioner.

PETITIONERS' BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

Supplementing their joint petition herein, and in support of same, petitioners respectfully state:

Opinion of the Court Below.

The opinion of the Court of Appeals for the Fourth Circuit, in these cases heard together, was rendered on January 27, 1932; is reported in 55 Fed. (2nd) 626, and appears at pages 120-134 of the Record.

The findings of fact and opinion of the United States Board of Tax Appeals were rendered on January 22, 1930, are reported in 18 B. T. A. 901, and appear at pages 37-57 of the Record.

Jurisdiction.

(*a*) The jurisdiction of this Court under Section 240 of the Judicial Code as amended (U. S. C., Title 28, Section 207) and under Section 1003(*a*) (*b*) of the Revenue Act of 1926 (44 St. (Part 2) 9, C 27) is invoked.

(*b*) The date of the decree of the Circuit Court of Appeals sought to be reviewed is January 27, 1932 (R. p. 135). A first petition for rehearing was overruled on March 7, 1932 (R. p. 170), and a second petition for rehearing was overruled on April 29, 1932, with stay of mandate for presentation of petition for certiorari on or before May 23, 1932 (R. p. 185). The

petition for certiorari was filed in this Court on May 23, 1932.

(*c*) These proceedings, originating in the United States Board of Tax Appeals, involve the power of the Commissioner of Internal Revenue to assess and collect additional income-excess taxes from these petitioners for 1919 to 1926 (R. p. 120, 132).

(*d*) The jurisdiction of this Court to review said proceedings is recognized in Rule 38 of this Court, and in *Old Colony Trust Co.* v. *Commissioner,* 279 U. S. 716, 727.

Statement of Case.

The full statement of essential facts made in the petition is here adopted in the interest of brevity.

Reasons for Review and Specifications of Error.

These are here repeated in substance as captions in the following

Argument.

Reason: The decision is contrary to the XVI Amendment and conflicts with decisions of this Court and of other Circuit Courts of Appeals on the same subject matter.

Questions:

1(*a*) *Whether the purchase money proceeds of sales of coal in place effected in* 1902 *and payable by the grantees in subsequent years in determinable amounts without interest as installments of said purchase money, are taxable income to petitioner company who,*

at and before March 1, 1913, *owned the unconditional claim then existing to recover or receive the unpaid part of said purchase money in the several subsequent years, and did thereafter collect same.*

1(*b*) *Whether the distribution of said proceeds to the stockholder Strother is taxable income to him.*

The lower court says (R. p. 123):

> "We shall assume for purposes of this decision, that the law of West Virginia is that a mining lease constitutes a sale of the mineral in place."

And therefore, we have sales of coal in place effected in 1902 for a consideration expressed in the contracts (R. 41) and payable to the grantor:

> —"Ten cents for each and every ton of coal mined"—and
>
> —"Five thousand dollars for each and every year as a minimum * * * whether the quantity of coal mined shall produce that amount of royalty or not."

Petitioner company never owned any coal in place, and in 1912 only succeeded to the claim of the grantor then and subsequently existing to receive and collect said payments in the later years.

The simple question from these undisputed facts is whether the XVI Amendment authorizes levy of income tax upon the subsequent receipt of proceeds of a claim existing on and before March 1, 1913, and it

is submitted same must be answered in the negative and contrary to the conclusion of the lower court.

The XVI Amendment "conferred no new power of taxation" (*Stanton* v. *Baltic Mining Company,* 240 U. S. 103, 110); it merely removed the principle of the *Pollock Case* (157 U. S. 429), that an income tax was a charge upon invested property and thereby was unconstitutional as a direct tax not apportioned, and that its enactment as an excise tax subject only to the constitutional rule of uniformity did not make it constitutional (*Brushaber* v. *Union P. R. Co.,* 240 U. S. 1, 18). In *Evans* v. *Gore,* 253 U. S. 245, 260, 261, the genesis of the Amendment is reviewed, including reference to the message of Governor Hughes to the New York Legislature expressing fear that the Amendment might extend to excepted subjects, and reference to the assurances to the contrary thereby obtained.

This Court has not precisely decided the question, but numerous decisions of lower courts hold that subsequent payments, resulting from a right to money established and accrued before the XVI Amendment, are not subject to income taxes, being only the return and collection of capital without income increment.

Thus, in *Saunders* v. *Commissioner,* 29 F. (2) 832, (C. C. A. 3), an inventor in 1911 sold an invention covered by a patent application and in 1920 received $25,000 in payment therefor, and it is held same was a return of capital and not taxable income. In *United States* v. *Guinzberg,* 278 F. 363 (C. C. A. 2), a dividend declared before March 1, 1913 is held not taxable income when thereafter received. In *Park* v. *Gilligan,*

293 Fed. 129, a claim for damages existing before and on March 1, 1913 and realized by payment in 1916 is held not to be income when distributed in dividends to stockholders. In *Schneider* v. *Duffy*, 43 F. (2) 642, taxpayer in 1916 agreed to accept 1,500 shares of stock, deliverable 300 shares per year as consideration for his certain agreements, and it was held any income from the transaction was received in 1916 and not when the stock was delivered.

In *Old Colony R. R. Co.* v. *Commissioner*, — U. S. — (52 S. Ct. 211), taxpayer had received bond premiums before 1913 and the regulations permitted same to be amortized over the life of the bond, but this Court said:

> "—these premiums could not be income for any other year than that in which they were received. That income had become capital prior to the adoption of the Amendment and could not be reached by a subsequent income tax act."

By analogy, herein the coal in place had been converted into the chose in action acquired by petitioner company before adoption of the Amendment, and its subsequent realization thereon is not income; if the bond premium contracted to be paid in 1904 in the cited case, was not collected until 1914, we have the present case.

In *Strattons Independence* v. *Howbert*, 231 U. S. 399, 414, 415, this Court said:

> "The sale outright of a mining property might fairly be described as a mere conversion of the capital from land into money."

In *Crile* v. *Commissioner*, 55 F. (2) 804 (C. C. A. 6), we read:

> "Where there is an intent to create in the 'lessee' an interest in the property itself—as by way of purchase—even though that interest may be forfeitable by failure to perform conditions subsequent, and this intent is made manifest by the instruments duly executed to carry it into effect, the attending payment is a return of capital, and should be so regarded, at least prior to forfeiture and reversion."

If the sale proceeds are not taxable income to the petitioner company, they are not taxable income to the petitioner Strother (Cf. *Park* v. *Gilligan, supra*).

It follows that the lower court erred in holding that purchase money proceeds of sales in place effected in 1902 constituted taxable income when collected in later years, and that its decision conflicts with decisions of this Court and other federal courts.

Question:

2. *Whether Congress intended by the Revenue Acts to tax said proceeds of sale.*

2(*a*). *Whether the grantor of coal sold in place is a lessor, and as such entitled to the statutory depletion allowances of a lessor.*

While conceding that sale of the coal in place was effected by the 1902 demise, the lower court contradicts this in (R. p. 124) deciding the vendor is a lessor entitled to depletion allowances for the return of capital

from the sale proceeds when collected. If said proceeds, as presented in the previous paragraph of this brief, are here held to be only the return of a capital claim existing and owned by petitioner before the Amendment, such conclusion becomes immaterial, but pending decision of that question, same must be considered.

In the first place, Congress could not tax the proceeds of the capital claim for reasons previously given. To do so violates the constitutional provisions which limit the power of Congress to tax income and no more, under the XVI Amendment.

This Court said in *Nichols* v. *Coolidge*, 274 U. S. 531, 541:

> —"under the mere guise of reaching something within its powers, Congress may not lay a charge upon what is beyond them. Taxes are very real things and statutes imposing them are estimated by practical results."

In the second place, as a sale in place is a severance of the estate of the grantor, such grantor is not a lessor, and as depletion is allowed by Congress only upon the taxpayer's interest in the mine, the grantor has no depletable interest after the sale in place was effected.

The lower court (R. p. 124) adverts to discussions by this Court of mining as a business in which both lessor and lessee are interested, but a grantor who receives royalties in return for the thing sold is not interested in the mining business. Here an estate, the coal in place, was sold. In *Burnet* v. *Logan*, 283 U. S. 404,

very similarly, taxpayer sold certain stock, taking payment in cash and royalties on ore mined; thereupon, the Commissioner sought to find income in the royalty receipts by allowance of depletion deductions, but this Court put aside the contention (page 412), saying:

> "The 1916 transaction was a sale of stock—not an exchange of property. We are not dealing with royalties or deductions from gross income because of depletion of mining property."

Petitioner here was not in the mining business because its predecessor had previously sold the coal in place to operators who mined same as their own, taking and retaining possession of the acreage and coal for that purpose in the ensuing years.

A sale of mineral in place effects a complete severance of the estate conveyed (*Group No. One Oil Corporation* v. *Bass*, 283 U. S. 279), wherein certain alleged immunities of a grantor were declared lost to its grantee, as distinguished from their preservation to a lessee in the later decision of *Burnet* v. *Coronado Oil and Gas Co.*, — U. S. — (decided April 11, 1932). The payments by the vendee for coal bought in place are capital expenditures and not the deductible rentals of a lessee (*Jefferson Gas Coal Co.* v. *Commissioner*, 52 F. (2) 120 (C. C. A. 3)).

Congress provides for allowance of depletion deductions only to the owner and to the lessor and lessee of a mine (Cf. Statute quoted in Appendix), and hence grants no depletion to a vendor after sale of his interest in the property. The depletion deduction is not a matter of right, and express authority therefor must

be found in the Revenue Acts (*Stanton* v. *Baltic M. Co.*, 240 U. S. 103; *Burnet* v. *Thompson Oil and Gas Co.*, 283 U. S. 301). The essential test is the interest of the claimant in the property, for as said in *Weiss* v. *Wiener*, 279 U. S. 333, 336 (quoted in other respects (as we believe erroneously) in the opinion below);

> —"he must show an interest in the property and a present loss to make the statute apply."

In *Darby Lynde Co.* v. *Commissioner*, 51 F. (2) 32 (C. C. A. 10) (Cert. denied 52 S. C. 40), the discovery value depletion basis available to a partnership is denied to a successor corporation created and owned by the partners. In *Pugh* v. *Commissioner*, 49 F. (2) 76 (C. C. A. 5) (Cert. denied, 52 S. C. 22), a taxpayer is held to have lost his right to depletion of his lease interest after conveyance of such interest on the ground he thereby has become a lessee without investment. In *South Vernon Oil Co.* v. *Hopkins*, 49 F. (2) 1028 (C. C. A. 5), we have the same conclusion and the reason stated that the sale severed the depletable interest in the property.

Third, in case of a severance of interest, of a sale, the Congress has in the Revenue Acts made other provisions, entirely apart from depletion, for taxing any capital gain. Thus, in Texas, where, as in West Virginia, the state rule of sale of mineral in place governs such matters, a taxpayer leased ⅞ of the mineral, while retaining the other ⅛ interest, and received a cash bonus and royalties. That he thus sold the ⅞ interest in place, making his bonus receipt subject to

the special tax rate upon a capital gain, and that his retained interest remained subject to depletion is the decision in *Ferguson* v. *Commissioner*, 45 F. (2) 573 (C. C. A. 5). In *Harmel* v. *Commissioner*, — F. (2) — (February 23, 1932) (C. C. A. 5), the same conclusion is reached upon authority of *Group No. One Oil Corporation* v. *Bass*, and other decisions of this Court. In *Alexander* v. *King*, 46 F. (2) 235, in a very similar case, the capital gain provision was held inapplicable because the Oklahoma rule of property does not recognize a sale of mineral in place and ascertains the parties to be lessor and lessee. (Cf. *Burnet* v. *Coronado Oil and Gas. Co.*, — U. S. — (*supra*).)

The lower Court (R. p. 124), after finding petitioner company stands in the shoes of a grantor and not of a lessor as the result of the sale in place, nevertheless decides that petitioner is a lessor and that the subsequent payments are income, on the ground (R. p. 124) that:

> "The federal courts must respect the local laws of property laid down by the courts of the state, but the power of Congress to tax must be judged by the realities of the situation and not by the logic of state rules of property, pushed inexorably to their extreme."

Such opinion conclusion flows from discussion of earlier decisions of this Court with especial emphasis upon cases in which certiorari was denied (R. p. 123), and the statement (R. p. 125) that later decisions of this Court (cited in the opinion), are not progressive to the acceptance of the state rule of property because (R. p. 125):

> —"it is obvious that each of these decisions turned upon the fundamental question whether the property sought to be taxed came within the purview of the taxing statutes."

Such precise fundamental question is the gravamen of this case, and the lower court—like the Board in its decision of this case—labors in a twilight of tax decisions now lifted by this Court. Such zone of error has arisen by acceptance of denials of certiorari as being a contradiction of previous decisions of this Court; notwithstanding, this Court has repeatedly declared a denial of certiorari does not have such an effect (*United States* v. *Carver,* 260 U. S. 482; *Atlantic C. L. Co.* v. *Powe,* 283 U. S. 401), and expresses no opinion upon the merits of said cases.

In other words, a supposed Federal rule of property, instead of the state rule of property, was reared by the Board as decisive herein of the taxability of the purchase money payments, and previously such supposed Federal rule had its effect upon the decision of Circuit Judge in the West Virginia litigation of petitioner (R. p. 50). The lower court restates and relies upon such rule herein as being established by numerous denials of certiorari (R. p. 123). The announcement of said Federal rule, as in disregard of the state rule, made in May, 1929 in *Hirschi* v. *United States,* 67 Ct. Cl. 637 (Cert. denied, 280 U. S. 576), is quoted (R. p. 51) in the Board opinion as follows:

> "The Federal Government is not limited in its selection of subjects for taxation by the construction of the State courts as to the property

> rights of individuals, provided the subject taxed was primarily a proper subject for taxation. *Congress in passing a revenue act does not, and is not called upon to suit the revenue system of the country to the varying and conflicting decisions and laws of the different states.*" (Italics supplied.)

This Federal rule of property found support in *Berg* v. *Commissioner*, 33 F. (2) 641 (Cert. denied, 280 U. S. 598), decided in June, 1929, and in the earlier decision of *Rosenberger* v. *McCaughn*, 25 F. (2) 699 (C. C. A. 3) (Cert. denied, 278 U. S. 604), and the Board decision in January, 1930, is thus but another expression of such rule. Afterwards, this Court definitely struck the rule down in *Poe, Collector* v. *Seaborn*, 282 U. S. 101, 117, saying:

> "Finally, the argument is pressed upon us that the Commissioner's ruling will work uniformity of incidence and operation of the tax in the various states, while the view urged by the taxpayer will make the tax fall unevenly on married people. * * * The answer to such argument, however, is that the constitutional requirement of uniformity is not intrinsic, but geographic. *Billings* v. *United States*, 232 U. S. 261; *Head Money Cases*, 112 U. S. 580; *Knowlton* v. *Moore*, 178 U. S. 41. And differences of state law, which may bring a person within or without the category designated by Congress as taxable may not be read into the Revenue Act to spell out a lack of uniformity. *Florida* v. *Mellon*, 273 U. S. 12."

Again this Court struck the rule down in the income tax case of *Phillips* v. *Commissioner*, 283 U. S. 589. It gave the state rule of sale in place full effect in the income tax case *Group One Oil Corp.* v. *Bass*, 283 U. S. 279. It upheld the state rule of property, but as sometimes unimportant, in the excise tax cases of *Tyler* v. *United States*, 281 U. S. 497; *Crooks* v. *Harrelson*, 282 U. S. 55; *Bromley* v. *McCaughn*, 280 U. S. 124.

In its decision of *Crooks* v. *Harrelson* (p. 63) this Court expressly disapproved *Steedman* v. *United States*, 63 Ct. Cl. 226 (Cert. denied 275 U. S. 528) upon which the Hirschi decision was substantially rested by the Court of Claims.

Adherence to state rules of property in determining the ownership of property as the base of liability for income taxes springs from early decisions of this Court (*McCormick* v. *Sullivant*, 10 Wheat. 192, 202; *United States* v. *Fox*, 4 Otto 315), and is precisely reflected in later decisions (*Poe* v. *Seaborn*, 282 U. S. 101).

Lastly, the ruling of the lower court herein is not logical in results. If notwithstanding a sale in place, the vendor is held entitled to depletion, although he has parted with the property, this conflicts with the established rule that depletion is incident to the property interest. It deprives the vendee, as the sole owner of the property, of some part of his depletion deduction. It turns his capital payments of installments of the purchase money into rentals in the hands of the recipient. It creates an allowance not authorized by law.

It is submitted the Congress did not intend to tax said purchase money receipts, and that the vendor is not a lessor entitled to depletion allowances; that the errors of the lower court in so holding are apparent and in substantial conflict with decisions of this and other Federal courts.

Reason 2. An important question of federal taxation is decided in a way in direct conflict with a decision of another Circuit Court of Appeals.

Question:

2(*b*) *Whether the excess amount of minimum payment received in any year from the grantee over the payment thereby made for coal actually mined within the year is subject to any depletion allowance.*

Any depletion allowable to petitioner company is limited by the lower court and Board to the payment measured by coal actually mined and paid for within any year, and thereby is disallowed upon any part of an annual minimum payment not representing coal mined. This limitation deprives petitioner company of depletion upon more than 2,000,000 tons of coal in the controversial years (R. pp. 160-1).

The Regulations of the Commissioner of Internal Revenue under the depletion section of the Revenue Acts allow consideration of bonus payments in computing the unit rate. The Board, in its decisions (R. p. 49), as applied herein, has disapproved the Regulations, and eliminated such bonus payments, meaning, in this case, payments not based upon coal actually

mined within the year. In this case, the Commissioner submitted a tax computation based upon the Board opinion with the protest that he stood committed to the principle (R. pp. 108, 157-8) of allowing depletion upon coal paid for instead of coal actually mined in a taxable year.

The lower Court herein, by affirming the Board, has approved its elimination of coal paid for but not mined as an element of the computation of depreciation. This question of defining the depletable base reached the Courts about the same time in the present case, and also in *Murphy Oil Company* v. *Burnet*, 55 F. (2) 17 (C. C. A.-9), wherein the Commissioner by cross petition for review raised the issue, and that Court reversed the Board and precisely decided the question on January 11, 1932, thereby entirely sustaining the regulations of the Commissioner. The opinion by Judge Wilbur is complete. The subsequent decision of January 27, 1932, herein, affirming the Board, places two Circuit Courts of Appeal in direct conflict upon this basic question affecting almost every lessor and lessee of a mineral deposit.

Reference is made to the argument of petitioners upon this conflict in their petition for rehearing (R. pp. 157-162).

Reason 3: The decision of a question of res adjudicata is probably untenable, and should be decided by this Court.

Question:

3. *Whether a judgment against a Collector, who was therein defended of record by the Commissioner of*

Internal Revenue, and which judgment involves the same subject matter of reasonable depletion as is presented herein, and was duly paid by the United States, is res adjudicata against the Commissioner as to the amount of depletion, if any, allowable to petitioner.

The undisputed facts (R. p. 47) are thus found by the Board:

> —"said judgment was duly paid by the United States. In said action the Bankers Pocahontas Coal Co., one of the petitioners herein, was plaintiff; plaintiff petitioner appearing in its own right and the collector as defendant, who was defended in said action by the United States District Attorney and the Solicitor of Internal Revenue (now General Counsel). In this proceeding and in said court action the subject matter of the action and of these proceedings is the same, namely, the depletion unit allowable in computing the amount of such depletion deduction as will return to the taxpayer the capital value existing in the coal content of the corporation's property as of March 1, 1913."

The lower Court (R. pp. 126-7) thus decides the question:

> "Hence the taxpayer claims that the question is no longer open between it and the Government, since it is a general principle that when a fact is distinctly put in issue, and directly determined by a court of competent jurisdiction between the parties in a law suit as a ground for recovery, it cannot be disputed in a subsequent suit between the same parties or their privies, even if the second suit is for a

different cause of action. *Southern Pacific R. R.* v. *U. S.*, 168 U. S. 1, 48; *New Orleans* v. *Citizens Bank*, 167 U. S. 371.

"The rule is applicable, however, only when the subsequent suit is between the same parties or their privies. The taxpayer maintains that we have had situation in the present litigation because the United States in reality is its opponent in both cases, being represented by the Collector of Internal Revenue in the prior suit, and by the Commissioner of Internal Revenue now. But the argument is refuted by the decision in *Sage* v. *United States*, 250 U. S. 33, where it was expressly ruled, against the protest of the Government, that the court was not bound by a judgment in a former suit concerning the same subject matter between the taxpayer and the Collector of Internal Revenue, because a suit against a Collector of Internal Revenue is personal and its incidents, such as the nature of the defenses open and the allowance, of interest, are different. This ruling has recently been cited with approval by the Supreme Court in *Graham & Foster* v. *Goodcell*, 282 U. S. 409, 430. The decision of the District Court for the Southern District of West Virginia was therefore not binding upon the Commissioner, and he had the authority to determine anew, as a question of fact, what allowance should be made for the depletion of the mine."

The opinion statement that taxpayer maintains "The United States in reality is its opponent in both cases" is, at most, derived from the amended petition (R. p. 19), stating:

> "That in the action aforesaid, and herein, the parties are identical, being petitioner suing in its own right, and the United States as defendant, represented respectively by its Commissioner of Internal Revenue, and by the respondent, Commissioner of Internal Revenue; that said action was defended for the United States by the United States District Attorney and by Robert A. Littleton, Special Attorney from the office of the General Counsel of the Commissioner of Internal Revenue which was known at said time as the Solicitor's office, as attorneys of record, and the details of defense and satisfaction of said judgment were handled by said Special Attorney, or Attorneys, representing the respondent herein."

But, if the *Sage* case decides the Collector of Internal Revenue is not the United States, it does not follow that the Commissioner of Internal Revenue is the United States—which is the erroneous deduction of the lower court here presented for review. In fact, whether the *Sage* case is *stare decisis* that a judgment against a Collector is not binding upon the United States, is open to examination. Therein, it appears taxpayer, having recovered a part of certain taxes against a Collector, was authorized by subsequent legislation to recover additional parts thereof from the United States. The Government relied upon the former judgment as a bar to the further recovery, notwithstanding the subsequent legislation, and compelled taxpayer to contend the judgment was no bar. Mr. Justice Holmes says (250 U. S. 33, 36-38):

> "The former judgment is not a bar."

and after proceeding with comment upon the status of an action against a Collector and the judgment therein, concludes:

> "But perhaps, it would be enough to say that if the judgment otherwise were a bar, the bar would be removed by the subsequent enactment of the Act of July 27, 1912, upon which, as well as upon the Act of 1902, this claim is based. * * * The Act of 1912, like that of 1902, created rights where they had not existed before, and the claimant's rights are not barred."

Petitioners submit this decides only that the subsequent legislation removed the alleged bar of the previous judgment. That such judgment against its officer constitutes no bar against the United States was entirely settled previously in *Carr* v. *United States*, 98 U. S. 433; in *United States* v. *Lee*, 106 U. S. 196, 222, and other decisions. In no wise does this *Sage* Case decide a taxpayer may not resist the Commissioner of Internal Revenue by claiming the parties settled the same issue in litigation between said taxpayer and a Collector whom the Commissioner defended. Yet the lower court has so held.

Briefly, the historical situation is that the Board of Tax Appeals has "appellate powers which are judicial in character" (*Blair* v. *Oesterlein Mach. Co.*, 27 U. S. 220), designed to afford taxpayers a redetermination of tax liabilities asserted by the Commissioner of Internal Revenue, and a further review of its decision in the Circuit Court of Appeals and in this Court (*Old Colony Trust Co.* v. *Commissioner*, 279 U. S. 716, 721).

By petition to the Board, the taxpayer in effect enjoins the Commissioner from assessment of tax pending subsequent judicial decision of the controversy. The Commissioner, sued therein as an officer of the United States, cannot successfully invoke the immunity of the United States (*United States* v. *Lee*, 106 U. S. 196; *Trudal* v. *Wesley*, 167 U. S. 204, 222; *Scranton* v. *Wheeler*, 179 U. S. 141, 153; *Wells* v. *Nickles*, 104 U. S. 444), nor is the immunity of the United States to be ascribed to such officer. The cited cases decided a judgment against its officer is not available against the United States.

There is a privity of duty between the Collector and Commissioner, notwithstanding they are separate officers, appointed by the President (R. S. 319, 3142); the Commissioner has general charge of the assessment and collection of taxes (R. S. 321), remits, refunds and pays back taxes illegally or erroneously collected, and repays the Collector all moneys recovered for taxes collected by him with the costs and expenses of suit (R. S. 3220); his discretion is not reviewable by any other officer of the Government (*Kaufman's Case*, 96 U. S. 568) and he may satisfy a judgment against a Collector without issue of a certificate of probable cause (*United States* v. *Frerichs*, 124 U. S. 315); the Collector gives bond in the amount prescribed by the Commissioner (R. S. 3143), sues for the recovery of taxes when authorized to do so by the Commissioner (R. S. 3214). A taxpayer may not sue a Collector to recover taxes except after previous presentation of his claim to the Commissioner (R. S. 3226). Thus both

are intimately related in their official duties, the Collector being substantially the agent of the Commissioner.

In *Second National Bank* v. *Woodworth, Collector,* 54 F. (2) 672, the Collector defended against the recovery of taxes on the ground claimant had previously been adjudged defeated in his prior action upon the same claim against the United States. The District Court, in finding the prior judgment protects the Collector as a Governmental agent and trustee, passes by the *Sage Case,* to rest its decision upon *Bank of Kentucky* v. *Stone,* 174 U. S. 799, wherein a decree enjoining a town from enforcing a tax was held to bar a similar proceeding against its board of assessors. In other words, the court holds that, although a judgment against an agent may not bind the principal, a judgment against a principal may be a bar as to an agent privy with such principal as to the subject matter in controversy.

In *Greylock Mills* v. *White,* 55 F. (2) 704, it is held that the judgment entered as the result of Board proceedings against the Commissioner, and judicial review thereof, is *res adjudicata* of all matters litigated therein, in a subsequent proceeding by the same taxpayer for recovery of the tax against a Collector. Thus, it is established by precedent that a Collector may invoke the protection of a judgment in favor of the United States or of the Commissioner involving the same taxpayer and same taxes.

But, herein, the West Virginia judgment is against the Collector, the agent, and not against his principals, either the United States or the Commissioner, and it appears the Commissioner joined with him and defended for him in perfect privity and concert against petitioner. To admit the resulting judgment is thereafter binding on both of them, does not concede or imply that it is likewise binding upon the United States, which neither consented to be sued in the proceeding, nor had declared by statute its responsibility for the resulting decree, as happened in *Minnesota* v. *Hitchcock,* 185 U. S. 373.

The privity of conduct between these officers established here of record must be ignored, in order to conclude that the judgment against the Collector is not binding upon the Commissioner of Internal Revenue, who assisted the Collector to defend the action—and this contradicts well recognized rules of law.

In *Beyer Co. v. Fleischmann Co.,* 15 F. (2) 465 (C. C. A. 6), where a similar situation prevailed, we read:

> "The general rule is that one who prosecutes or defends a suit in the name of another, to establish or protect some interest of his own, *or who openly assists in an action in aid of some such interest,* to the knowledge of the opposing party, is as much bound by the judgment as he would be if he had been a party of record. *Penfield* v. *Potts & Co.* (6 C. C. A.), 126 F. 475, 61 C. C. A. 351; *Greenwich Ins. Co.* v. *Friedman Co.* (6 C. C. A.), 142 F. 944, 74 C. C. A. 114; *Foote* v. *Parson, etc.* (6 C. C. A.), 196 F. 951, 118 C. C. A. 105; *Southern Pacific R. Co.* v. *United States,* 168 U. S. 1, 18 S. Ct. 18, 42 L. Ed.

355; *Souffront* v. *La Compagnie Des Suereries*, 217 U. S. 475, 30 S. Ct. 608, 54 L. Ed. 846." (Italics supplied.)

In *Souffront* v. *Compagnie*, 217 U. S. 475, 487, the same rule is again stated:

> "*The persons for whose benefit, to the knowledge of the court and of all the parties to the record, litigation is being conducted, cannot, in a legal sense, be said to be strangers to the cause.* The case is within the principle that one who prosecutes or defends a suit in the name of another, to establish and protect his own right, *or who assists in the prosecution or defense of an action in aid of some interest of his own, and who does this openly, to the knowledge of the opposing party*, is as much bound by the judgment, and as fully entitled to avail himself of it, as an estoppel against an adversary party, as he would be if he had been a party to the record. *Lovejoy* v. *Murray*, 3 Wall. 1, 18 L. Ed. 129." (Italics supplied.)

The lower court therefore erred in holding the Commissioner of Internal Revenue was entitled to the immunity of the United States, and, failure to give effect to the established facts as to the privity of the Collector and Commissioner is in conflict with the foregoing decisions of this Court and other Federal courts.

Conclusion.

The lower court decision operates to defeat the correct tax of net income contemplated by the Revenue Acts in this:

It purposes to tax as income a flow of wealth not taxable under the XVI Amendment.

It nullifies basic rules of property whereby income subject to tax is ascertained, and raises other rules not justified by the law or precedents.

It causes confusion in the property rights of taxpayers, and tends to injustice in the imposition of taxes.

It lays improper burdens upon taxpayers, both upon corporations and individual stockholders.

It produces a lack of uniformity in decisions of the several Circuit Courts of Appeals upon fundamental matters of taxation.

It tends to the continuance of litigation by not giving conclusive effect to judgments in proceedings involving the same subject matter between the same parties and their privies.

Petitioners therefore respectfully insist that the writs, here prayed for, should issue, and upon final hearing that the judgments of the Circuit Courts of Appeals for the Fourth Circuit should be reversed with proper directions that justice may prevail.

Respectfully submitted,

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

MASON, SPALDING AND McATEE,
GOODYKOONTZ AND SLAVEN,
Of Counsel.

APPENDIX.

Constitution, Statutes and Regulations Involved.

The Constitution of the United States.

Amendment XVI (effective March 1, 1913).—The Congress shall have power to lay and collect taxes on incomes from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration.

Individual Gross Income.

Revenue Act of 1918—Section 213 (40 Stat. 1057-96, C. 18):

> "That for the purposes of this title (except as otherwise provided in section 233) the term 'gross income'—
>
> "(*a*) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * *, of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever."

Revenue Act of 1921—Section 213 (same as above). (42 Stat. 227, C. 136.)

Revenue Act of 1924—Section 213 (same as Revenue Act of 1918 above). (43 Stat. 253, C. 234.)

Revenue Act of 1926—Section 213 (same as Revenue Act of 1918 above). (44 Stat. (Part 2) 9, C. 27.)

Individual Net Income.

Revenue Act of 1918—Section 212 (*Idem.*):

> "That in the case of an individual the term 'net income' means the gross income as defined in section 213, less the deductions allowed by section 214."

Revenue Act of 1921—Section 212 (same as Revenue Act of 1918 above). (*Idem.*)

Revenue Act of 1924—Section 212 (same as Revenue Act of 1918 above). (*Idem.*)

Revenue Act of 1926—Section 212 (same as Revenue Act of 1918 above). (*Idem.*)

Corporation Gross Income.

Revenue Act of 1918—Section 233 (*Idem.*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'gross income' means the gross income as defined in section 213, except that:" (Exceptions not material.)

Revenue Act of 1921—Section 233 (*Idem*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'gross income' means the gross income as defined in sections 213 and 217, * * *." (Not material here.)

Revenue Act of 1924—Section 233 (same as Revenue Act of 1921 above). (*Idem.*)

Revenue Act of 1926—Section 233 (same as Revenue Act of 1921 above). (*Idem.*)

Corporation Net Income.

Revenue Act of 1918—Section 232 (*Idem*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233 less the deductions allowed by section 234, and the net income shall be computed on the same basis as is provided in subdivision (*b*) of section 212 or in section 226." (Omitted as relating only to accounting method.)

Revenue Act of 1921—Section 232 (*Idem*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233 less the deductions allowed by section 234."

Revenue Act of 1924—Section 232 (same as Revenue Act of 1921 above). (*Idem.*)

Revenue Act of 1926—Section 232 (same as Revenue Act of 1921 above). (*Idem.*)

Meaning of Net Income.

Article 21—(Reg. 45, years 1918, 1919, 1920) (Reg. 62, years 1921, 1922, 1923) (Reg. 65, year 1924) (Reg. 69, years 1925, 1926):

> "The tax imposed by the statute is upon income. In the computation of the tax various classes of income must be considered:
>
> "(*a*) Income (in the broad sense), meaning all wealth which flows in to the taxpayer other

than as a mere return of capital. It includes the forms of income specifically described as gains and profits, including gains derived from the sale or other disposition of capital assets. Cash receipts alone do not always accurately reflect income, for the statute recognizes as income-determining factors other items, among which are inventories, accounts receivable, property exhaustion, and accounts payable for expenses incurred. * * *

"(*b*) Gross income, meaning income (in the broad sense) less income which is by statutory provision or otherwise exempt from the tax imposed by the statute. * * *

"(*c*) Net income, meaning gross income less statutory deductions. The statutory deductions are in general, though not exclusively, expenditures, other than capital expenditures, connected with the production of income. * * *

"(*d*) Net income less credits. * * *

"The surtax is imposed upon net income; the normal tax upon net income less credits. Although taxable net income is a statutory conception, it follows, subject to certain modifications as to exemptions and as to deductions for partial losses in some cases, the lines of commercial usage. Subject to these modifications statutory 'net income' is commercial 'net income.' This appears from the fact that ordinarily it is to be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer. As to the net income of corporations, see section 232 * * * and article 531."

Article 531—(Same Regulations):

Net income.—Net income is that portion of the gross income which remains after all proper deductions have been taken into account. The net income of corporations is determined in general in the same manner as the net income of individuals, but the deductions allowed corporations are not precisely the same as those allowed individuals. * * * The net income of corporations is to be computed on the same basis as to accounting periods as the net income of individuals."

Article 90—(Same Regulations):

Income accrued prior to March 1, 1913.—Any claim existing unconditionally on March 1, 1913, whether presently payable or not and held by a taxpayer prior to March 1, 1913, whether evidenced by writing or not, and all interest which had accrued thereon before that date, do not constitute taxable income, although actually recovered or received subsequent to such date. Interest accruing on or after that date is taxable income. Where an interest-bearing claim held on February 28, 1913, is paid in whole or in part after that date, any gain derived from the payment of the claim is taxable. The amount of such gain is the excess of the proceeds of the claim (both principal and interest) exclusive of any interest accrued since February 28, 1913, already returned as income, over the cost thereof (both principal and interest then accrued). However, the gain to be included in gross income where the fair market value of the claim as of March 1, 1913, is greater than

the cost thereof, is the excess of the amount received over such value. In the case of an insurance policy its surrender value as of March 1, 1913, may be used as a basis for the purpose of ascertaining the gain derived from its sale or other disposition. Where services were rendered prior to March 1, 1913, but paid for thereafter, the amount received is taxable income to the extent of the excess of such amount over the fair market value on March 1, 1913, of the principal of the claim and any interest which had then accrued."

Corporation Deductions.

Revenue Act of 1918—Section 234:

"That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions: * * *

"(9) In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost including cost of development not otherwise deducted: *Provided*, That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: * * * In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee;"

Revenue Act of 1921—Section 234 (same as Revenue Act of 1918 above). (*Idem.*)

Revenue Act of 1924—Section 234 (same as Revenue Act of 1918 above). (*Idem.*)

Revenue Act of 1926—Section 234 (same as Revenue Act of 1918 above). (*Idem.*)

Article 204—(same Regulations as above):

> "*Amount returnable through depletion and depreciation in the case of lessor.*—(*a*) In the case of a lessor, the amount remaining in any year returnable through depletion and depreciation deductions is (1) the value of his equity in the property at the basic date minus (2) depletion and depreciation sustained, whether legally allowable or not, from the basic date to the taxable year, plus (3) subsequent allowable capital additions, and minus (4) the value of the land at the basic date for other purposes than mineral production and the residual value of other property at the end of operations. The amount returnable through depletion is the total capital remaining less the sum recoverable through depreciation. The provisions of this paragraph do not apply to the computation of the depletion allowance in the case of oil and gas wells when such allowance is based on the income from the property.
>
> "(*b*) The values of the equities of lessor and lessee shall be computed separately, but, when determined as of the same basic date, shall together never exceed the value at that date of the property in fee simple. * * *
>
> "(*d*) The value of the lessor's equity in a mineral property under lease March 1, 1913, for the entire operating life of the mineral deposits is to be taken to mean (1) the cost or (2) the value as of March 1, 1913, of the royalties and

other payments to be expected under the terms of the lease in effect on that date, whichever is greater."

Article 215 (Regulations 45, 62, 65 above):

Depletion-Adjustments of accounts on bonus or advanced royalty.—(*a*) Where a lessor receives a bonus or other sum in addition to royalties, such bonus or other sum shall be regarded as a return of capital to the lessor, but only to the extent of the capital remaining to be recovered through depletion by the lessor at the date of lease. If the bonus exceeds the capital remaining to be recovered, the excess and all the royalties thereafter received will be income and not depletable. If the bonus is less than the capital remaining to be recovered by the lessor through depletion, the difference may be recovered through depletion deductions based on the royalties thereafter received. The bonus or other sum paid by the lessee for a lease made on or after March 1, 1913, will be his value for depletion as of date of acquisition."

Article 216 (215) (Regulations 69 above amending Article 215):

Depletion-Adjustments of accounts based on bonus or advanced royalty.—(*a*) Where a lessor receives a bonus in addition to royalties, there shall be allowed as a depletion deduction in respect of the bonus an amount equal to that proportion of the cost or value of the property on the basic date which the amount of the bonus bears to the sum of the bonus and the royalties expected to be received. Such allowance shall be deducted from the amount remaining to be

recovered by the lessor through depletion, and the remainder is recoverable through depletion deductions on the basis of royalties thereafter received."

Dividends.

Revenue Act of 1918—Section 201 (Idem):

"(*a*) That the term 'dividend' when used in this title (except in paragraph (10) of subdivision (*a*) of section 234) means (1) any distribution made by a corporation, other than a personal service corporation, to its shareholders or members, whether in cash or in other property or in stock of the corporation, out of its earnings or profits accumulated since February 28, 1913 * * *.

"(*b*) Any distribution shall be deemed to have been made from earnings or profits unless all earnings and profits have first been distributed. * * *

"(*c*) Any distribution made during the first sixty days of any taxable year shall be deemed to have been made from earnings or profits accumulated during preceding taxable years; but any distribution made during the remainder of the taxable year shall be deemed to have been made from earnings or profits accumulated between the close of the preceding taxable year and the date of distribution, to the extent of such earnings or profits, and if the books of the corporation do not show the amount of such earnings or profits, the earnings or profits for the accounting period within which the distribution was made shall be deemed to have been accumulated ratably during such period."

Revenue Act of 1921—Section 201 (Idem):

"(*a*) That the term 'dividend' when used in this title (except in paragraph (10) of subdivision (*a*) of section 234 and paragraph (4) of subdivision (*a*) of section 245) means any distribution made by a corporation to its shareholders or members, whether in cash or in other property, out of its earnings or profits accumulated since February 28, 1913. * * *

"(*b*) For the purposes of this Act every distribution is made out of earnings or profits, and from the most recently accumulated earnings or profits, to the extent of such earnings or profits accumulated since February 28, 1913; but any earnings or profits accumulated or increase in value of property accrued prior to March 1, 1913, may be distributed exempt from the tax, after the earnings and profits accumulated since February 28, 1913, have been distributed. * * *

"(*f*) Any distribution made during the first sixty days of any taxable year shall be deemed to have been made from earnings or profits accumulated during preceding taxable years; but any distribution made during the remainder of the taxable year shall be deemed to have been made from earnings or profits accumulated between the close of the preceding taxable year and the date of distribution, to the extent of such earnings and profits, and if the books of the corporation do not show the amount of such earnings or profits, the earnings or profits for the accounting period within which the distribution was made shall be deemed to have been accumulated ratably during such period.

This subdivision shall not be in effect after December 31, 1921."

Revenue Act of 1924—Section 201 (same as Revenue Act of 1921 above). (*Idem.*)

Revenue Act of 1926—Section 201 (same as Revenue Act of 1921 above). (*Idem.*)

Article 1542—(same Regulations):

"*Source of Distribution.*—For the purpose of income taxation every distribution made by a corporation is made out of earnings or profits to the extent thereof and from the most recently accumulated earnings or profits."

Article 1543—(same Regulations):

"*Distribution Out of Earnings or Profits Accumulated Prior to March* 1, 1913.—Any distribution by a corporation out of earnings or profits accumulated prior to March 1, 1913, or out of increase in value of property accrued prior to March 1, 1913 (whether or not realized by sale or other disposition prior to or on or after March 1, 1913), is not a dividend within the meaning of Title II. The provisions of the preceding sentence shall be applied uniformly to cases arising under the Revenue Act of 1916, the Revenue Act of 1917, the Revenue Act of 1918, the Revenue Act of 1921, and the Revenue Act of 1924, as well as the Revenue Act of 1926. A corporation cannot distribute earnings or profits accumulated or increase in value of property accrued prior to March 1, 1913, exempt from tax, unless and until all earnings or profits accumulated since February 28, 1913, have been distributed. * * *

"In determining whether a dividend is out of earnings or profits accumulated since February 28, 1913, or prior to March 1, 1913, due consideration must be given to the facts, and mere bookkeeping entries increasing or decreasing surplus will not be conclusive. * * *"

Article 1546—(same Regulations):

"*Distributions from Depletion or Depreciation Reserves.*—A reserve set up out of gross income by a corporation and maintained for the purpose of making good any loss of capital assets on account of depletion or depreciation is not a part of surplus out of which ordinary dividends may be paid. * * * No distribution, however, can be made from such a reserve until all the earnings or profits of the corporation have first been distributed."

FILE COPY

JUL 16

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104.

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

No. 105.

D. J. F. STROTHER, PETITIONER,

v.

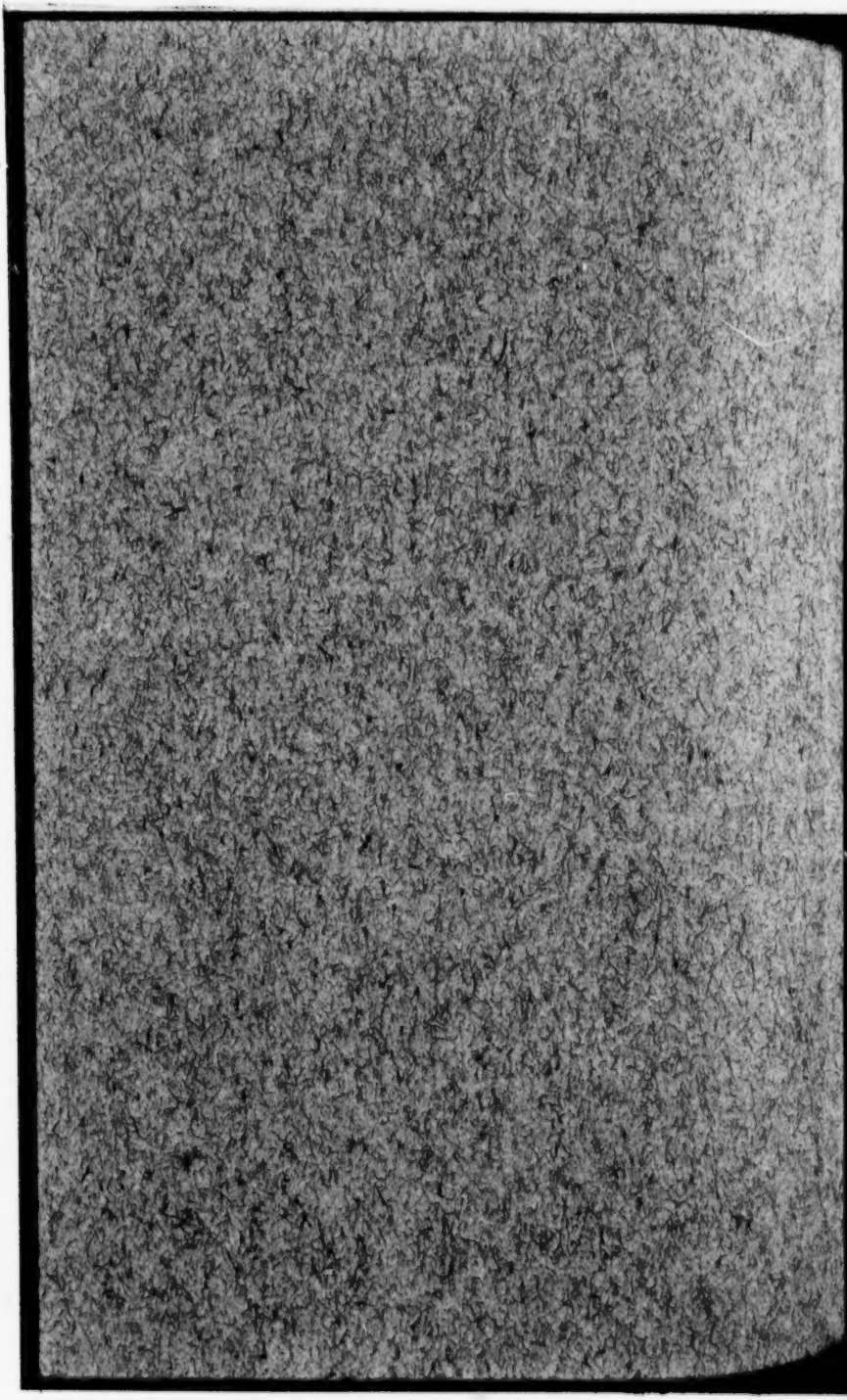
DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

RESPONSE OF PETITIONERS TO OPPOSITION BRIEF OF RESPONDENT.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

MASON, SPALDING & McATEE,
GOODYKOONTZ AND SLAVEN,
Of Counsel.



INDEX.

Subject Index.

	Page
Introduction	1
Granted certioraris not distinguishable	2
No sufficient opposition	2
The facts	2
The issues—*Basically*, a constitutional and statutory issue	3
Alternatively, the basis of depletion and *res adjudicata*	3
Argument—*Basically:*	
Error in holding sale proceeds to be taxable lease royalties	4
Same not taxable	4
State rule of property controls	4
Conflict of decisions	4
Respondent does not justify lower court	5
Citations not in point	5
No lease nor royalties in present case	6
Constitutional conflict	7
Harmel decision applicable	8
Argument—*Alternatively:*	
Minimum payments are cash bonuses	10
Murphy Oil decision applicable	10
Res adjudicata unanswered	11
Conclusion	11

Citations.

Burnet v. Logan, 283 U. S. 404	4
Burnet v. Thompson Oil & Gas Co., 283 U. S. 301	5
Crile v. Commissioner, 55 F. (2) 804 (C. C. A. 6)	7
Crooks v. Harrelson, 283 U. S. 56	6
Darby Linde Co. v. Commissioner, 51 F. (2) 32 (C. C. A. 10) cert. denied	5
Ferguson v. Commissioner, 45 F. (2) 573 (C. C. A. 5)	6, 9
Group No. 1 Oil Corp. v. Bass, 283 U. S. 279	4, 5, 6, 7, 8
Harmel v. Commissioner, 52 F. (2) 153 (Burnet v. Harmel No. 26, on certiorari)	2, 3, 5, 6, 9
Hirschi v. United States, 67 Ct. Cl. 637	6

Page

Jefferson Gas Coal Co. v. Commissioner, 52 F. (2) 120..... 4, 6, 7
McLean v. United States, 226 U. S. 374..... 7
Murphy Oil Co. v. Burnet, 55 F. (2) 17 (No. 80, on certiorari) 2, 3, 10
Pugh v. Commissioner, 51 F. (2) 32 (C. C. A. 10) (cert. denied) 5
Saunders v. Commissioner, 29 F. (2) 832..... 4
Schneider v. Duffy, 43 F. (2) 642..... 4
South Vernon Oil Co. v. Hopkins, 49 F. (2) 1628 (C. C. A. 5).. 5
Stanton v. Baltic M. Co., 240 U. S. 103..... 5
Steedman v. United States, 63 Ct. Cl. 226..... 6
Stratton's Independence v. Howbert, 231 U. S. 209..... 4, 5, 7
United States v. Guinzberg, 293 F. 129..... 4
Von Baumbach v. Sargent Land Co., 242 U. S. 503..... 5

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104.

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,
v.
DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

No. 105.

D. J. F. STROTHER, PETITIONER,
v.
DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE.

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT.

RESPONSE OF PETITIONERS TO OPPOSITION BRIEF OF RESPONDENT.

Supplementing their petition for certiorari, and responsive to the opposition brief of respondent, peti-

tioners suggest that certiorari has been granted in two of the decisions relied upon by petitioners, which are not distinguishable from the present case as contended by respondent, and that respondent shows no substantial reason for opposing grants of certiorari herein.

The writs have been granted in *Harmel* v. *Commissioner*, 56 F. (2d) 153, on April 18, 1932 (now pending as *Burnet* v. *Harmel, No.* 26, *October Term,* 1932), and in *Murphy Oil Co.* v. *Burnet*, 55 F. (2d) 17, on May 31, 1932 (now pending as *No.* 80, *October Term,* 1932).

The application of the same principles to these cases and to the *Harmel* and *Murphy* cases would doubtless have changed the result in one of the two sets of cases, notwithstanding any due allowance for differences in facts.

Under such circumstances, grant of certiorari herein is submitted to be just and proper.

Summary of Facts.

The tax-liability of petitioner Strother rises or falls with that of petitioner Coal Company, as its stockholder, and need not be discussed in detail.

Briefly, the predecessors of petitioner Coal Company as owners in fee of West Virginia acreage, valueless except for its coal content, sold said coal content in place, in 1901 and 1902, to certain operators for a consideration of "ten cents for each and every ton of coal mined" and "$5,000 for each and every year as a minimum" (Petition, p. 15), and retained no interest in said coal content. In 1912, petitioner Coal Company was organized, and acquired the fee to said acreage

subject to said contracts, and the beneficial interest of its predecessors to collect and receive said contract considerations in the subsequent years, and, having no other business, has so collected them, and distributed them, upon a cash basis, to its stockholders. Thus, neither its predecessors nor petitioner Coal Company were ever in the mining business, and have only collected the deferred proceeds of a sale of real estate as effected and completed in 1902.

The Issues.

Petitioner Coal Company therefore submits said sale receipts (*Harmel case, supra*), are not ordinary income subject to income tax, but are mere naked receipts of a claim existing unconditionally on and before March 1, 1913, and thereafter collected, which Congress cannot subject to income taxes. Alternatively, if said receipts be taxable as royalties subject to depletion allowances, petitioner Coal Company submits the cash bonuses derived from minimum royalties (*Murphy Oil case, supra*) are depletable, and the rate of depletion is *res adjudicata* from prior litigation.

ARGUMENT.

Said proceeds of sale are not taxable lease-royalties as held by the lower court.

The Circuit Court of Appeals held the 1902 contracts constituted a sale of the mineral in place under the law of West Virginia (R., p. 123). It only remained (upon

authority of *Stratton's Independence* v. *Howbert,* 231 U. S. 399; *Saunders* v. *Commissioner,* 29 F. (2) 832 (C. C. A., 3); *United States* v. *Guinzberg,* 278 F. 363 (C. C. A., 2); *Park* v. *Gillican,* 293 F. 129; *Schneider* v. *Duffy,* 43 F. (2) 642 (Cf. Petitioners' Brief, pp. 16, 17); (*Burnet* v. *Logan,* 283 U. S. 404) (Cf. Petitioners' Brief, p. 20)) for the Court to say the sale proceeds received in the later years were not taxable because they were the subsequent collections of a claim existing at and before the enactment of the XVIth Amendment.

But the Court erroneously said Congress intended to and does tax said receipts as royalties of a lessor subject to the statutory depletion deductions (R., p. 124), thus raising the primary constitutional and statutory questions. As mere sale proceeds established before the amendment and subsequently received as a return of capital, they were not taxable, and as the proceeds of a severance of interest, which is not the realization of capital and income from any retained interest in the property, they are not the royalties of a lessor. If the lower court is not in error, then a vendor or vendee (under the State law), in West Virginia, Pennsylvania and Texas of mineral in place is a lessor or lessee (under the Federal Revenue Acts), in Washington, D. C., and entitled there to the privileges of a lessor or lessee, viz., to any immunity of the lessor from tax, which is denied in *Group No.* 1 *Oil Corp.* v. *Bass,* 283 U. S. 279, to deductions of capital payments as rentals paid by a lessee which is denied in *Jefferson Gas Coal Co.* v. *Commissioner,* 52 F. (2) 120 (C. C. A.,

3), to treat a sale in place as a retained interest, which is denied in *Group One Oil Corp.* v. *Bass* (*supra*), and *Harmel* v. *Commissioner* (*supra*). If the lower court is not in error, then these decisions are wrong, as well as those cited above to establish that the proceeds of this particular sale in place are not taxable. If the lower court is not in error, the statutory allowance of depletion, only to the owner of a mineral property or equitably to the lessor and lessee of same upon their apparent interests in said property, is meaningless, which is denied in *Stanton* v. *Baltic M. Co.*, 240 U. S. 103, and *Burnet* v. *Thompson Oil and Gas Co.*, 283 U. S. 301, wherein depletion is declared not a matter of right and to be only authorized by the Revenue Acts; if the lower court is not so in error, a sale does not sever the depletable interest and deprive the vendor thereof, which is denied in *Darby Linde Co.* v. *Commissioner*, 51 F. (2) 32 (C. C. A., 10) (Cert. denied, 52 S. C. 40), in *Pugh* v. *Commissioner*, 49 F. (2) 76 (C. C. A., 5) (Cert. denied, 52 S. C. 22); *South Vernon Oil Co.* v. *Hopkins*, 49 F. (2) 1028 (C. C. A., 5), and *Group No. One Oil Corp.* v. *Bass*, 283 U. S. 279.

Respondent does not justify the ruling of the lower court.

Respondent in opposition (p. 9) says the authority and intention of Congress to tax the sales proceeds is upheld in *Stanton* v. *Baltic M. Co.*, 240 U. S. 103; *Stratton's Independence* v. *Howbert; Von Baumbach* v. *Sargent Land Co.*, and other decisions cited by the lower court (R., p. 123), in that they decide *royalties received*

under leases are income. But only two of these decisions affect instruments constituting a sale of mineral in place under the law of the State where same was situate. These are the *Hirschi* case from Texas, which is now contradicted by *Ferguson* v. *Commissioner,* 45 F. (2) 573 (C. C. A., 5), by *Group No. One Oil Corp.* v. *Bass* (*supra*), which respondent accepts, and by *Harmel* v. *Commissioner* (*supra*), in which respondent has obtained certiorari; and the *Roseberger* case from Pennsylvania, which has been broken down by *Jefferson Gas Coal Co.* v. *Commissioner,* 52 F. (2) 120 (C. C. A., 3). The *Steedman* case (Cert. denied, 275 U. S. 528) relied upon in the *Hirschi* decision is expressly disapproved in *Crooks* v. *Harrelson,* 282 U. S. 56, 63 (Cf. Petitioners' Brief, pp. 23-25), and *Ferguson* v. *Commissioner,* expressly and effectively distinguishes the *Stanton* decision by use of the same quotation (Opposition, p. 9) exhibited by respondent. Herein, the respondent's proposition, *royalties received under leases are income,* is without application, for there are *no leases,* and on the contrary *a sale in* 1902, and there are no royalties, for as said in the *Ferguson* opinion:

> —"royalties represent the retained interest of the lessor or the vendor in the property or minerals which he receives from time to time as revenues under the contract. He (Ferguson) did not convey that interest under the deed or lease, but provided that he should receive a fraction of the minerals themselves as produced * * *."

Consequently, the instant outright payment by the operators of 10 cents per ton of coal mined is not a royalty, but is a capital payment as said in *Burnet* v. *Logan* (*supra*), and *Jefferson Gas Coal Co.* v. *Commissioner* (*supra*) (Cf. Petitioners' Brief, pp. 19, 20).

That a sale in place effects a severance of the interest of the vendor is the State rule of property upheld in income tax cases from Texas (*Group No. One Oil Corp.* v. *Bass*), from Pennsylvania (*Jefferson Gas Coal Co.* v. *Commissioner*), and it remains to correct the erroneous conclusion of the lower court that, notwithstanding such serverance, the vendor and assigns retain a depletable interest in the property sold. It being true, as often decided by this Court, that the Revenue Acts are subject to State rules of property (Cf. Petitioners' Brief, pp. 24, 25) in ascertaining the ownership of property and defining income therefrom, it is evident error for the lower court to say the Revenue Acts require State rules of property to be ignored; for, as said in *McLean* v. *United States,* 226 U. S. 374, 382:

> "To decide otherwise is to say that Congress gave a right and took it away in the same instant."

Having here a completed sale of the property (Cf. *Strattons Independence* v. *Howbert* and *Crile* v. *Commissioner,* Petitioners' Brief, pp. 17, 18), with no retained interest and no income resulting from any use of the property, which sale was effected before the amendment, the decision of the lower court that sale-proceeds thereafter received are lease royalties subject to income tax conflicts with previous decisions of this

Court and denies the constitutional rights of petitioner.

Respondent errs in attempting to distinguish the Harmel case, in which certiorari has been granted.

The present case is identical with the *Ferguson* and *Harmel* cases when read in connection with *Group No. One Oil Corp.* v. *Bass,* 283 U. S. 279, decided in the interval between them. Herein, all coal in place was demised for a consideration of "10 cents for each ton mined"; *Ferguson,* in Texas, leased his property for oil production for a consideration of "the equal one-eighth of all oil produced and saved", and a cash consideration (20 B. T. A. 130); *Harmel,* in Texas, leased his property for "stipulated royalties and a cash consideration (19 B. T. A. 376); *Group One,* in Texas, leased State property for "the value of one-eighth of the petroleum produced" (*supra*). The *Group One* decision by this Court, in deciding the sale in place divested the property of its previous ownership and incident tax immunity, adopts the Texas law that:

> "They (the leases) do not authorize the purchaser to take and use 7/8ths or any other mere fractional part of the oil or gas in the land leased. The purchaser instead buys all the oil and gas, for a stipulated price, part of the price being measured by the value of a certain fraction of the produced oil and gas, which is a very different thing from the value of that fraction of the oil and gas in place. *The leases conveyed all the oil and gas* in granting the right to find, produce, and appropriate all of them, *in consider-*

ation of the payment of stipulated sums and also the value of a stated fraction of the oil and gas produced.'' (Italics supplied.)

It seems clear the *Ferguson* and *Group One* contracts are within this rule, and reference to the *Harmel* record also shows the "equal one-eighth" as in the *Ferguson* case. It follows that in each case the consideration was, as stated by this Court, "stipulated sums and also the value of a stated fraction of the oil and gas produced" (*supra*). This means a deferred payment as in the present case, payable on production of the mineral, and that the cases are identical. In the *Ferguson* and *Harmel* cases this was not recognized or claimed by taxpayers, and the court was led to conclude the one-eighth was a retained interest subject to depletion. This attitude, error though it may be, does not distinguish the *Ferguson* or *Harmel* cases from the present case, for herein, as in the *Group One* case, there is no retained interest. Respondent argues it exists, because in the *Ferguson* and *Harmel* cases a retained interest is recognized to exist, and because herein there are deferred payments. But *Group One* rests upon a consideration deferred in its entirety, and, being a sale in place, the deferment of the consideration does not militate against the severance of interest thereby consummated in the execution and delivery of the instrument of sale.

The alternative position of petitioners.

The primary position of petitioner Coal Company is that the sale proceeds of the contract consummated

before the amendment are not taxable when thereafter received. If they are taxable as royalties subject to depletion, the alternative questions of the sufficiency of depletion allowances are presented. The Board and lower court refused to allow depletion upon bonus payments, being the excess of the annual minimum payments over coal actually mined, whereby depletion is denied upon over 2,000,000 tons of coal paid for but not mined in the years in controversy (Cf. Record, pp. 160, 161), and refused to allow depletion at the rate previously adjudged in litigation between the parties.

Respondent errs in attempting to distinguish the Murphy Oil case, in which certiorari has been granted.

Respondent (Opposition, p. 15) entirely misconceived any alleged conflict of the present case with the *Murphy Oil Company* case, wherein the Circuit Court of Appeals held a cash bonus was subject to depletion allowances and reversed the Board rulings which the Court of Appeals herein has sustained. Petitioner Coal Company here received the minimum annual payment as a cash bonus to the extent that the operator could not mine coal equal to such payment, and upon this ground, affirmed by the lower court (R., p. 132), that such excess cash payment is a bonus, not being a payment for coal actually mined, depletion on such bonus is herein denied (R., p. 49). That makes the present case identical with the *Murphy Oil* case in which certiorari has been allowed.

Respondent makes no answer to the res adjudicata issue.

Upon the *res adjudicata* issue respondent (Opposition, pp. 16-17) merely reiterates the Court of Appeals' reasoning (Petitioners' Brief, pp. 28, 29) which petitioner has fully discussed in its supporting brief (Petitioners' Brief, pp. 30-35). No reexamination of the assertions is necessary under these circumstances.

Conclusion.

Petitioners respectfully represent they are informed the custom of this Court is to grant certiorari when it appears certiorari has been granted and is pending in similar cases, as is here apparent.

For this, and the reasons originally stated in their petition and supporting brief, they respectfully insist the writ should issue herein as prayed in their petition.

Respectfully submitted,

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

FILE COPY

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE.

No. 105

D. J. F. STROTHER, PETITIONER,

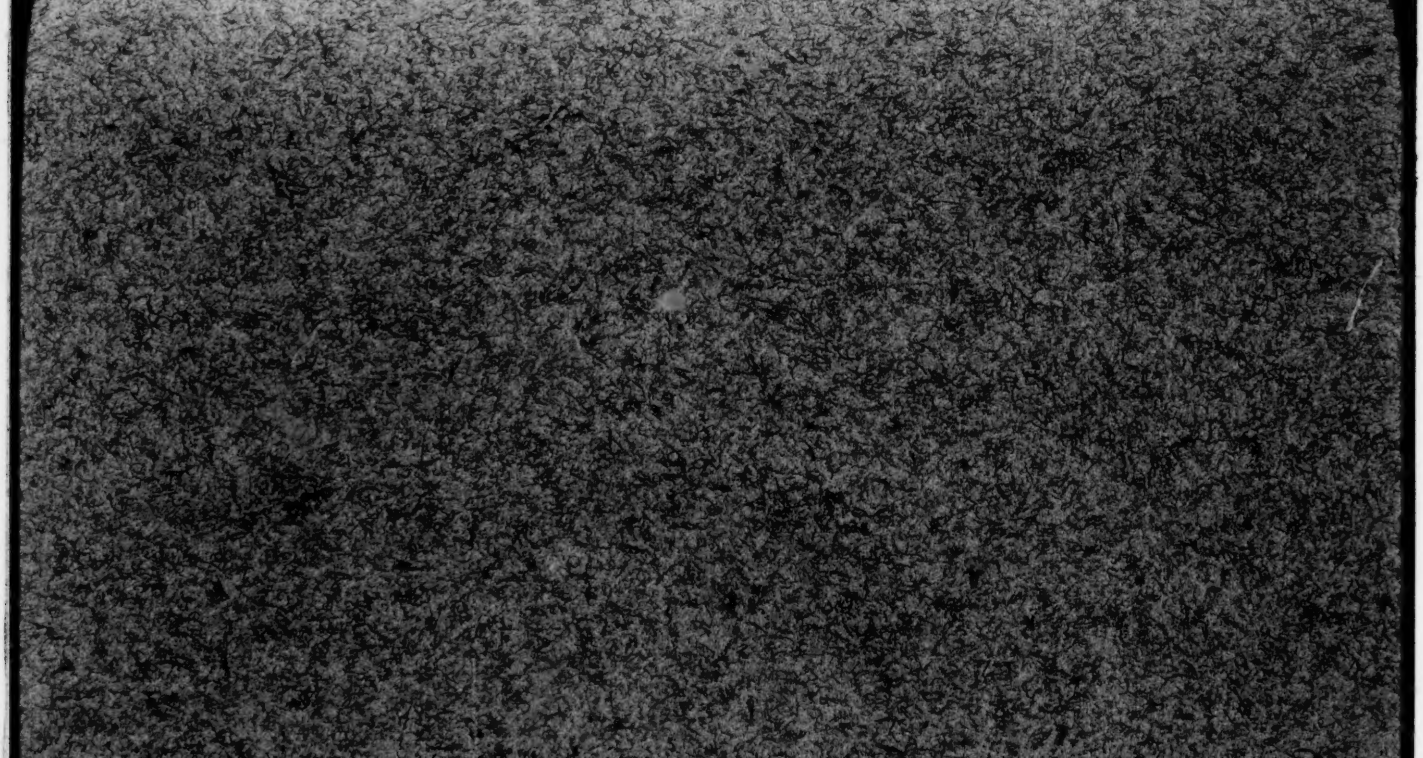
vs.

COMMISSIONER OF INTERNAL REVENUE.

PETITIONERS' BRIEF.

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

Of Counsel:
GOODYKOONTZ AND SLAVEN,
MASON, SPALDING & McATEE.



INDEX

Subject Index.

	Page
Grant of the writs	1
Opinions below and jurisdiction	2
The basic issues	2
Statement of the case	3
The material facts	3
Proceedings before the Board of Tax Appeals	6
Proceedings in the Circuit Court of Appeals	7
Errors to be urged	8
Summary of argument	9
Argument	10
Conclusion	45

Decisions Cited.

Alexander v. King, 46 F. (2) 235	22, 24
Atlantic C. L. Co. v. Powe, 283 U. S. 401	24
Baldwin v. Md., 179 U. S. 220	39
Bedell v. Commissioner, 30 F. (2) 622 (C. C. A.-2)	14, 16
Berg v. Commissioner, 33 F. (2) 641 (Cert. denied 280 U. S. 598)	24, 25
Beyer v. Fleischmann, 15 F. (2) 465 (C. C. A.-6)	38
Billings v. United States, 232 U. S. 261	26
Blair v. Oesterlein M. Co., 275 U. S. 220	41
Bromley v. McCaughn, 280 U. S. 124	30
Brushaber v. Union Pac. R. Co., 240 U. S. 1	29
Burnet v. Coronado Oil & Gas Co., 283 U. S. 393	20, 22
Burnet v. Logan, 283 U. S. 404	11, 14, 15
Burnet v. Logan, 42 F. (2) 193	16
Burnet v. Thompson Oil & Gas Co., 283 U. S. 301	21
Burkett v. Commissioner, 31 F. (2) 667	24
Carr v. United States, 98 U. S. 433	43
Coal Co. v. Overholt, 81 W. Va. 427	10
Commissioner v. Brown, 54 F. (2) 563 (C. C. A.-1)	11
City of New Orleans v. Citizens Bank, 167 U. S. 371	39
Crile v. Commissioner, 55 F. (2) 804 (C. C. A.-6) (Cert. denied October 10, 1932)	11
Crocker v. Malley, 249 U. S. 223	38, 44

Page

Crooks v. Harrelson, 282 U. S. 35..... 24, 26, 27
Darby Lynde Co. v. Commissioner, 51 F. (2) 32 (C. C. A. 10) (Cert. denied 52 S. C. 40)..... 21
Doyle v. Mitchell, 247 U. S. 179..... 13
Feather v. Baird, 85 W. Va. 267..... 10
Ferguson v. Commissioner, 45 F. (2) 573 (C. C. A.-5)..... 18, 22
Florida v. Mellon, 273 U. S. 12..... 26
Graham & Foster v. Goodcell, 282 U. S. 409..... 36
Greylock Mills v. White, 55 F. (2) 704..... 45
Group No. One Oil Corp. v. Bass, 283 U. S. 279....19, 20, 22, 24, 26, 27
Guinter v. Atlantic C. L. R. Co., 200 U. S. 273..... 39
Harmel v. Commissioner, 55 F. (2) 153 (C. C. A.-5)..... 22
Head Money Cases, 112 U. S. 580..... 26
Hirschi v. United States, 67 Ct. Cl. 637 (Cert. denied 280 U. S. 576)..... 6, 24, 25, 27
Jefferson Gas Coal Co. v. Commissioner, 52 F. (2) 120 (C. C. A. 3)..... 20
Kaufman's Case, 96 U. S. 568..... 40
Knowlton v. Moore, 178 U. S. 41..... 26
Kosmeryl v. Commissioner, 25 F. (2) 87 (C. C. A.-7)..... 16
Lucas v. Alexander, 279 U. S. 573..... 12, 45
Lucas v. American Code Co., 280 U. S. 455..... 14
Lynch v. Allworth Stevens Co., 267 U. S. 364..... 29
McCormick v. Sullivant, 10 Wheat, 192..... 27
Murphy Oil Co. v. Burnet, 55 F. (2) 17 (C. C. A.-9).....21, 33, 34, 35
Nichols v. Coolidge, 274 U. S. 531..... 20
N. Y. C. & H. R. R. R. Co., v. United States, 24 Ct. Cl. 22..... 43
Old Colony R. R. Co. v. Commissioner, 284 U. S. 552..... 12, 17
Old Colony Trust Co. v. Commissioner, 279 U. S. 716..... 41
O'Meara v. Commissioner, 34 F. (2) 390 (C. C. A.-10)..... 17
Pacific Gas Co. v. San Francisco, 265 U. S. 403..... 16
Park v. Gilligan, 293 F. 129..... 13
Phillips v. Commissioner, 283 U. S. 589..... 26
Poe v. Seaborn, 282 U. S. 101.....24, 26, 27, 32
Poindexter v. Greenhow, 114 U. S. 270..... 42
Pugh v. Commissioner, 49 F. (2) 76 (C. C. A.-5) (Cert. denied 52 S. C. 22)..... 22
Rosenberger v. McCaughn, 25 F. (2) 699 (C. C. A.-3) (Cert. denied 278 U. S. 604).....23, 25, 27
Sage v. United States, 250 U. S. 33..... 36
Saunders v. Commissioner, 29 F. (2) 832 (C. C. A.-3)..... 13
Schneider v. Duffy, 45 F. (2) 642..... 13
Schnell v. Cochran, 107 U. S. 625..... 43
Second Nat. Bank v. Woodworth, 54 F. (2) 672..... 44

Page

Smith v. Root, 66 W. Va. 633 10
Souffront v. LeCompagnie, 217 U. S. 475 38
South Vernon Oil Co. v. Hopkins, 49 F. (2) 1028 (C. C. A.-5) 22
Stanton v. Baltic Mining Co., 240 U. S. 103 ..... 21, 23, 29
Steedman v. United States, 63 Ct. Cl. 226 (Cert. denied 275 U. S. 528) 27
Stratton's Independence v. Howbert, 231 U. S. 399 ..... 12, 23, 28, 31
Toothman v. Courtenay, 62 W. Va. 167 10
Tyler Admr. v. United States, 281 U. S. 497 ..... 24, 26
United States v. Biwabik Mining Co., 247 U. S. 116 29
United States v. Carver, 260 U. S. 482 24
United States v. Fox, 4 Otto. 315 27
United States v. Guinzberg, 278 F. 363 (C. C. A.-2) 13
United States v. Frerichs, 124 U. S. 315 ..... 40, 43
United States v. Sherman, 98 U. S. 565 42
United States v. Stone and Downer Co., 274 U. S. 225 39
Urpman v. Lowther Oil Co., 53 W. Va. 501 10
Von Baumbach v. Sargent Land Co., 242 U. S. 503 ..... 23, 28
Weiss v. Weiner, 279 U. S. 333 21

CONSTITUTION AND STATUTES CITED.

Constitution, Amendment XVI 4, 5, 8, 9, 10, 17, 20, 28, 47

Individual Gross Income.

R. A. 1918, Section 213 (40 St. L. 1057-96, C. 18) 47
R. A. 1921, Section 213 (42 St. L. 227, C. 136) 47
R. A. 1924, Section 213 (43 St. L. 253, C. 234) 47
R. A. 1926, Section 213 (44 St. L. (Part 2) 9, C. 27) 47

Individual Net Income.

R. A. 1918, Section 212 (Idem as above) 48
R. A. 1921, Section 212 48
R. A. 1924, Section 212 48
R. A. 1926, Section 212 48

Corporation Gross Income.

R. A. 1918, Section 233 (Idem as above) 48
R. A. 1921, Section 233 48
R. A. 1924, Section 233 48
R. A. 1926, Section 233 48

Corporation Net Income.

Page
R. A. 1918, Section 232 (Idem as above) 49
R. A. 1921, Section 232 49
R. A. 1924, Section 232 49
R. A. 1926, Section 232 49

Meaning of Net Income.

Article 21 (Reg. 45, 62, 65, 69) 49
Article 531 (Reg. 45, 62, 65, 69) 50

Income Accrued Prior to March 1, 1913.

Article 90 (Same) 51

Corporation Deductions (Depletion).

R. A. 1918, Section 234 (Idem as above) 52
R. A. 1921, Section 234 52
R. A. 1924, Section 234 52
R. A. 1926, Section 234 52

Returnable to Lessor.

Article 204 (Same) 52

Adjustments as to Bonus.

Article 215 (Reg. 45, 62, 65) 53
Article 216 (Reg. 69) 34, 35, 54

Dividends.

R. A. 1918, Section 201 (Idem as above) 55
R. A. 1921, Section 201 55
R. A. 1924, Section 201 56
R. A. 1926, Section 201 57

Sources of Distribution.

Article 1542 (Same) 57
Article 1543 (Same) 57

Distribution from Depletion Reserves.

Article 1546 (Same) 58

Certificate of Probable Cause.

Page
R. S. 989 (12 St. L. 741, C. 76, 12) 58

Refunding Taxes and Penalties Including Judgments.

R. S. 3220 (14 St. L. 111, C. 184, 9; 17 St. L. 401, C. 13, 1; 40 St. L. 1145, C. 18, 1316 (a); 44 St. L. 115, C. 27, 1111; 45 St. L. 878, C. 852, 619; 45 St. L. 996, C. 901, 3..... 58

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE.

No. 105

D. J. F. STROTHER, PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE.

PETITIONERS' BRIEF.

Grant of the Writs.

Writs of certiorari to the Circuit Court of Appeals, Fourth Circuit, were granted herein on October 10, 1932, and the two cases, being related, should be heard together.

Opinions Below and Jurisdiction.

The opinion of the Circuit Court of Appeals rendered January 27, 1932, is reported in 55 F. (2) 626 (R., pp. 120-134); the findings of fact and opinion of the United States Board of Tax Appeals, rendered January 22, 1930, are reported in 18 B. T. A. 901 (R., pp. 30-57). The jurisdiction herein has been shown heretofore (Petition for writ and supporting brief (pp. 1, 2, 13)).

The Basic Issues.

Whether proceeds of a sale of coal in place effected in 1902 and collected subsequent to the Sixteenth Amendment under contracts not providing for production of any maximum or minimum tonnage, or for any definite payments, constitute taxable net income under the several Revenue Acts.

Whether the statutory depletion allowances available to a lessor are allowable to a vendor of coal in place who has severed his interest in the depletable mineral, or to his assignee.

Whether the statutory depletion allowances available to a lessor are applicable to payments for coal in excess of the payment for coal actually mined within a taxable year.

Whether a depletion allowance determined in prior litigation between a taxpayer and Collector of Internal Revenue, who was defended therein by the Commissioner of Internal Revenue, constitutes *res adjudicata* in these later proceedings between the same taxpayer and the Commissioner of Internal Revenue.

Statement of the Case.

Income tax deficiencies of $39,171.05 against petitioner Company, for the years 1920 to 1926, and of $5,806.11, against petitioner Strother, are here involved.

In 1901 and 1902, the fee owner of West Virginia acreage, valueless except for its coal content (R., p. 39), demised and let said coal content to various mining operators. The instruments of demise and letting were originally prepared by petitioner Strother as attorney for said fee owners, and their form is that prevailing in the West Virginia coal fields, adopting and following the Pennsylvania form of contract as introduced by Pennsylvanians who were largely instrumental in the early development of the West Virginia coal fields. One of the instruments, agreed upon as typical of all of them, is in evidence herein (R., p. 40). The Board of Tax Appeals admitted (R., p. 49), and the lower court herein expressly held (R., p. 123), that said instrument constitutes a sale of coal in place under the State law of West Virginia and of Pennsylvania.

In 1912, petitioner Company was organized and acquired, and has since held, the fee title to said acreage subject to said instruments, and also the beneficial interest of the former fee owner in said instruments. By said typical instrument the mining operator in 1901 agreed to pay "10 cents per ton for each and every ton of coal mined", with "$5,000 for each and every year as a minimum" (R., pp. 40-41),

and the grantor retained no interest in said coal content. Petitioner Company, having no other business, has, since 1912, collected the contract payments each year (R., p. 90), and distributed them, upon a cash basis (R., p. 46), to its stockholders, of whom petitioner Strother is representative, excepting amounts necessary to meet the taxes herein involved which were retained and paid out at the first opportunity (R., p. 72).

The operators since 1901 and 1902 have possessed and mined the coal (R., pp. 39, 90).

Neither petitioner Company, nor the original fee-owner, were ever in the mining business; petitioner Company having acquired, in 1912, the rights to the subsequent payments for coal sold in 1902, never owned any coal, and, in subsequent years, only collected the deferred proceeds of sale of real estate effected and completed in 1901.

After adoption of the Sixteenth Amendment and enactment of the Revenue Acts, both petitioners in their tax returns disclosed said payments and distributions as being the proceeds of sales of coal in place effected before the Amendment, and consequently not subject to tax (R., pp. 38, 46, 49). Ignoring the state law of property (R., p. 92), the Commissioner of Internal Revenue for the years 1914-1919 held petitioner Company and the operators for Federal tax purposes were lessor and lessees, and said payments were gross income but that every 10-cent payment should be reduced by a statutory depletion allowance of 3.6 cents, representing the non-taxable return of capital or in-

vested property therein received, to ascertain taxable net income. Said Commissioner assessed and required petitioner Company thereby to pay taxes of about $6,000 to the proper collector upon the alleged net income so ascertained (R., pp. 47, 90). Petitioner Company, thereupon, sued said Collector in the United States District Court in West Virginia to recover said taxes for cause, either that same were the non-taxable proceeds of purchase money contracted for before the Sixteenth Amendment, existing unconditionally on March 1, 1913, and payable thereafter (R., p. 47), or alternatively, if petitioner Company was a lessor and not a vendor, that the depletion unit measuring return of capital or invested property should be fixed in a greater amount (R., p. 47). In said action the Commissioner of Internal Revenue by his own counsel of record, and the District Attorney defended the Collector (R., p. 47). Therein, petitioner Company obtained a final judgment fixing a depletion unit of 5 cents per ton, with a consequent recovery of a substantial part of the taxes, which judgment was duly satisfied and has since remained in full effect (R., p. 47).

Contemporaneous with and subsequent to said litigation, said Commissioner determined income taxes of about $40,000 (R., p. 38) against petitioner Company for the years 1920-1926, holding petitioner Company as a lessor was only entitled to depletion of 3.6 cents per ton, for 1920 to 1923, inclusive, and an average of 2.6 cents per ton of coal paid for in 1924 to 1926, inclusive (R., p. 75), and refusing to give any effect to the 5-cent depletion rate established by said

judgment (R., pp. 46, 47, 48) except in the computation of invested capital for 1920.

As to petitioner Strother, the Commissioner increased his net income for the several years by his entire receipts from said purchase money distributions, without any allowance for non-taxable depletion reserves received in the distributions, and determined the resulting deficiencies of tax against him (R., pp. 48, 49).

Petitioners, by their appropriate appeals, petitioned the United States Board of Tax Appeals for redeterminations of said several deficiencies, claiming petitioner Company was neither the owner nor lessor of any mine, neither petitioner was taxable upon purchase money payments derived from sales of coal in place effected before March 1, 1913, and payable thereafter without income increment, and claiming—in the alternative—that if the payments were taxable after allowance of depletion deductions, the 5-cent depletion rate established in previous litigation between the parties was *res adjudicata* thereof, and should be allowed instead of the 3.6-cent rate (R., pp. 7, 8, 18, 19). The Board of Tax Appeals, without denying that the demise of 1902 effected a sale of coal in place according to the property rule of West Virginia (R., p. 49), held: *First,* The contracts for Federal tax purposes, under the rule of *Hirschi* v. *United States, infra,* established the relation of lessor and lessee between petitioner Company and the operator, making the payments gross income subject to depletion allowances (R., p. 50); *Second,* That bonuses, or minimum payments in excess of payment of coal actually mined in

the year, are gross income not subject to depletion allowances (R., pp. 49, 70); and *Third,* The depletion rate of 5 cents per ton determined in previous litigation between the parties over the same subject matter was not thereby allowances to petitioner Company (R., p. 52), and said Board determined total deficiencies of $39,171.05 against petitioner Company (R., p. 71), and thereby of $5,806.11 against petitioner Strother.

By their petitions for review (R., p. 73) petitioners applied to the Circuit Court of Appeals for the Fourth Circuit for review of said Board decision, alleging as errors: (1) That such payments were not taxable income (R., p. 81); (2) Alternatively, that the adjudged 5-cent depletion rate was applicable (R., p. 81); and (3) That any depletion was allowable upon coal paid for and not merely upon coal mined (R., p. 82); and, (4) As to petitioner Strother, that he received no taxable income, or if so, that all depletion reserves should be eliminated from the distributions made to him.

The Circuit Court of Appeals held, *First,* the contracts of 1902 effected sales of coal in place (R., p. 123); *Second,* that, nevertheless, Congress intended to tax said sales proceeds by returning capital through lessor depletion allowances (R., p. 124); *Third,* that the West Virginia judgment was not binding upon the Commissioner and hence did not establish the 5-cent depletion rate (R., p. 127); and *Fourth,* affirmed the Board determination whereby the minimum annual payments in excess of payment for coal actually mined were held to be bonuses returnable as gross income without allowance of depletion deductions against

same (R., p. 132). It further held its decision of the Company case (R., p. 132) would substantially determine the Strother case. Incidental issues not here of importance are omitted as immaterial.

Thereupon, writs of certiorari were granted herein to each petitioner.

Errors to be Urged.

The Board and court below erred (references to opinion of each):

1. In deciding purchase money installments of the proceeds of sales of coal in place effected in 1901 and 1902, when paid by the grantees in the years subsequent to the Sixteenth Amendment, are taxable income to petitioner Company, who, at and before March 1, 1913, owned the unconditional claim and right then existing to receive the unpaid part of said purchase money in the several subsequent years, and thereafter merely collected same (R., pp. 49, 124).

1(*b*). In deciding the distribution by petitioner Company of said proceeds to its stockholder Strother is taxable income to him (R., pp. 57, 135).

2. In deciding Congress intended by the Revenue Acts to tax said proceeds of sale (R., p. 124).

3. In deciding the grantor of coal sold in place, or his assignee, is a lessor entitled to the depletion allowances prescribed for a lessor (R., pp. 51, 124) by the Revenue Acts.

4. In deciding that the excess amount of minimum payment received in any year from the grantee over

the payment therein made for coal actually mined within the year is not subject to any depletion allowance (R., pp. 49, 134).

5. In deciding a judgment in favor of petitioner Company against a Collector, who was defended of record in the proceeding by the Commissioner of Internal Revenue, acting through his official counsel, and which judgment involves the same subject matter of statutory depletion allowances as is presented herein, and was duly paid by the United States, is not *res adjudicata* herein against said Commissioner as to the amount of depletion, if any, allowable to petitioner Company (R., pp. 52, 127).

Summary of Argument.

The primary position of petitioners is that the proceeds of the sales of coal in place, effected before the Sixteenth Amendment was enacted, are not income subject to tax under the subsequent Revenue Acts when collected thereafter.

Their secondary or alternative position involves the sufficiency of statutory depletion allowances, if said proceeds subsequently received are royalties of a lessor subject to depletion. Petitioners contend any applicable depletion rate must be applied to the entire proceeds and not to the part of same only representing coal mined within the year. They further contend any depletion should be at the rate previously adjudged in litigation between the parties.

Decision of these issues in the case of petitioner Company will apply to and decide the case of petitioner Strother.

ARGUMENT.

Proceeds of the sale of mineral in place effected before the XVI Amendment and collected thereafter are not taxable as income to either petitioner under subsequent Revenue Acts, because they are only the returns from a claim or right unconditionally existing on and before March 1, 1913, and thereafter payable.

To hold otherwise conflicts with the XVI Amendment and judicial precedents.

Petitioners stand first upon the proposition of law announced by the Circuit Court of Appeals, to wit:

> "We shall assume for purposes of this decision that the law of West Virginia is that a mining lease constitutes a sale of the mineral in place."

In support thereof, the lower Court makes reference to *Coal Company* v. *Overholt,* 81 W. Va. 427, 424; *Feather* v. *Baird,* 85 W. Va. 267; *Urpman v. Lowther Oil Co.,* 53 W. Va. 501; *Toothman* v. *Courtney,* 62 W. Va. 167, and *Smith* v. *Root,* 66 W. Va. 633.

It follows the original fee owner sold the coal in place in 1901 and 1902 for a price payable thereafter, and petitioner Company in 1912 succeeded to and since holds the right to collect the unpaid purchase money in subsequent years. Said right involved no payment of interest or profit. The subsequent proceeds are clearly not subject to income tax, being within the definition of Article 90 of Regulations 45, 62, 65 and 69, issued by the Commissioner of Internal Revenue in

the years 1918 to 1926, inclusive. Said Article 90 provides:

> "Income accrued prior to March 1, 1913.—Any claim existing unconditionally on March 1, 1913, whether presently payable or not and held by a taxpayer prior to March 1, 1913, whether evidenced by writing or not, and all interest which had accrued thereon before that date, do not constitute taxable income, although actually recovered or received subsequent to such date. Interest accruing on or after that date is taxable income. Where an interest-bearing claim held on February 28, 1913, is paid in whole or in part after that date, any gain derived from the payment of the claim is taxable."

Here it may be noted that the foregoing Article has been broadened beyond "any claim existing unconditionally" by judicial interpretation, and in *Commissioner* v. *Brown*, 54 F. (2d) 563 (C. C. A. 1) such claim, *existing as a conditional obligation*, on and before passage of the Sixteenth Amendment, is held not to be income, when subsequently collected, upon authority of *Burnet* v. *Logan*, 283 U. S. 404, which latter decision of this Court is a sufficient touchstone to solve the present cases. Nor because the typical instrument provides a possible forfeiture upon defaults by the operators, can it be inferred the instrument creates a conditional obligation defeating the transfer of interest effected through the sale in place, for in *Crile* v. *Commissioner*, 55 Fed. (2d) 804 (C. C. A. 6) (certiorari denied October 10, 1932), wherein a sum of money was paid as part consideration of a lease, the Court says:

> "Where, there is an intent to create in the 'lessee' an interest in the property itself—as by way of purchase—even though that interest may be forfeitable by failure to perform conditions subsequent, and this intent is made manifest by the instruments duly executed to carry it into effect, the attending payment is a return of capital, and should be so regarded, at least prior to forfeiture and reversion."

It follows petitioner Company, as assignee of its predecessor who effected the sale, collects capital and no more in receipt of payments made since 1912 and after the Sixteenth Amendment.

The adoption of the Amendment makes March 1, 1913, when it became effective, the line of division between income that is not or is taxable under the subsequent Revenue Acts levying income taxes without apportionment, and it follows that any income previously existing was and is not subject to subsequent income taxes (*Lucas* v. *Alexander,* 279 U. S. 573, 577). This principle expressed in the foregoing Article has very recently found terse statement again by this Court in *Old Colony R. R. Co.* v. *Commissioner,* 284 U. S. 552, 557:

> "That income had become capital prior to the adoption of the Amendment and could not be reached by a subsequent income tax act."

Stating the proposition of fact more precisely in reference to the present case, we submit this Court said in *Strattons Independence v. Howbert,* 231 U. S. 399, 414-15:

> "The sale outright of a mining property might fairly be described as a mere conversion of the capital from land into money."

whereby, in this case, the subsequent collection of money resulting from a sale of property made before the Amendment became effective is a receipt of capital and not of income subject to tax under the subsequent Revenue Acts.

In the lower Courts, in similar situations, it has often been so decided. Thus, in *Saunders* v. *Commissioner,* 29 F. (2d) 832 (C. C. A. 3), an inventor, in 1911, sold an invention covered by a patent application, and, in 1920, received $25,000 in payment therefor, and it is held same was a return of capital and not taxable income. In *United States* v. *Guinzberg,* 278 F. 363 (C. C. A. 2), a dividend declared before March 1, 1913, is held not taxable income when thereafter received. In *Park* v. *Gilligan,* 293 Fed. 129, a claim for damages existing before and on March 1, 1913, and realized by payment in 1916 is held not to be income when distributed in dividends to stockholders. In *Schneider* v. *Duffy,* 43 F. (2d) 642, taxpayer, in 1916, agreed to accept 1,500 shares of stock deliverable 300 shares per year as consideration for his certain agreements, and it is held any income from the transaction was received in 1916 and not when the stock was delivered.

Petitioner Company is certainly entitled to return of its capital before taxable income is realized (*Doyle* v. *Mitchell,* 247 U. S. 179, 185), but the capital value on March 1, 1913, of its right to receive the purchase

money payable thereafter is not definitely known and cannot be ascertained as a matter of market value for reasons given in *Bedell* v. *Commissioner,* 30 F. (2d) 622, 624 (C. C. A. 2), as follows:

> "If a company sells out its plant for a negotiable bond issue payable in the future, the profit may be determined by the present market value of the bonds. But if land or a chattel is sold, and title passes merely upon a promise to pay money at some future date, to speak of the promise as property exchanged for the title appears to us a strained use of language, when calculating profits under the income tax.
>
> "* * * it is absurd to speak of a promise to pay a sum in the future as having a 'market value', fair or unfair. Such rights are sold, if at all, only by seeking out a purchaser and higgling with him on the basis of the particular transaction."

In *Burnet* v. *Logan,* 283 U. S. 409, 412, this Court held that the market value of an agreement to pay to taxpayer a certain sum per ton of extracted ore could not be determined, saying:

> "The lease contract did not require production of either maximum or minimum tonnage, or any definite payments. * * *
>
> "* * * a promise to pay indeterminate sums of money is not necessarily taxable income. 'Generally speaking the income tax law is concerned only with realized losses, as with realized gains.'" *Lucas* v. *American Code Co.,* 280 U. S. 455, 449.

In *Burnet* v. *Logan* a depletion rate computed upon conjecture is expressly rejected, and the 3.6 cent rate herein is therefore to be denied. Its basis is in substance the assumption that the present value of $34,000 being payment at the rate of 10 cents per ton receivable during each of 40 years after March 1, 1913, is $510,000, or 3.6 cents per ton on that date. But such assumption is not justified for no average receipt per year can be determined, and without an average annual receipt there can be no computation. No average annual receipt can be known for no maximum payment is provided, and the minimum is evidently not the measure of the receipt. Therefore, no actual market or fair value as of March 1, 1913, can be known for the contingencies of receipt remain undiscovered. Other material contingencies, default of the operator, possible acceleration of payment, uncertainty of production, and similar details, are entirely evident, and make the assumed value entirely fantastic, where petitioner Company is entitled to reality of computation.

The lower Court says an allowance of 3.6 cents per ton would return to taxpayer a total of $1,353,911.11 of capital upon the tonnage estimated in the stipulation as existing on March 1, 1913. The record shows (R., p. 44) petitioner Company through 1919 had only received $244,094.62, and that the capital value of $510,000 on March 1, 1913, does not include two coal seams which were being mined when the valuation was made (R., pp. 93, 102). This Court says in *Burnet* v. *Logan* (p. 412), a taxpayer is entitled to the return of capital before it may be charged with taxable income,

and where the capital is not in fact returned there is no taxable income.

The self-evident conjectural and speculative nature of any computed value on March 1, 1913, of the purchase money contracts is probably best visualized by reference again to the character of payment which justifies such computation. Such a comparative exists in *Kosmeryl* v. *Commissioner,* 25 F. (2d) 87 (C. C. A. 7), relating to sale of a mineral property before March 1, 1913, for a price payable in 40 equal installments, evidenced by non-interest bearing negotiable notes; and therein the present value of the notes on March 1, 1913, is declared to be their capital asset value and subsequent receipts in excess thereof to be taxable income. This accords with the statement of Judge Hand in *Bedell* v. *Commissioner, supra,* distinguishing such a case from one, such as the present case, involving a mere promise to pay money at a future date.

Herein, as in *Burnet* v. *Logan,* 42 F. (2d) 193, 196, the reasoning of the Circuit Court subsequently approved by this Court is entirely applicable where the duration of the mining operations, tonnage to be mined and receipts in any year, are all uncertain and therefore afford no basis of computation. The Court said:

> "The ultimate duration of the life of a mine is uncertain or unknown and forms no basis on which to formulate a definite financial policy. Hoover's Principles of Mining, p. 44. See also *Pacific Gas Co.* v. *San Francisco,* 265 U. S. 403. Moreover, the division of percentage as a return of capital and that of income is an estimate based upon assumptions and uncertainties. It is an unsafe guide either to determine ex-

> changeable value or the fair market value. *O'Meara* v. *Commissioner,* 34 F. (2d) 390 (C. C. A. 10.)"

Therefore, an income situation not being reasonably presented herein, it follows that Article 90 reasonably says taxable income or gain is not received when the claim is collected subsequent to the Amendment. This accords with the principles of *Old Colony R. R. Co.* v. *Commissioner,* 284 U. S. 552, 560, 561, that a construction of the taxing act most favorable to taxpayers in cases of doubt is proper and that:

> "The plain obvious and rational meaning of a statute is always to be preferred to any curious, narrow minded sense that nothing but the exigency of a hard case and the ingenuity and study of a powerful intellect would discover."
> * * *
> "* * * the words of the statute do not refer to some esoteric concept derived from subtle and theoretic analysis."

Taxation of any part of said contract proceeds as income being not authorized by the Sixteenth Amendment, or the subsequent judicial precedents, the contrary decision of the lower Court is material error.

Under subsequent Revenue Acts Congress never intended to tax the proceeds of this sale in place effected before the Amendment when thereafter collected, or to declare the vendor or his assignee is entitled to the statutory depletion allowances provided for a lessor of coal mines.

After holding the typical instrument constitutes a sale of coal in place, the lower court declares (R., p.

122) this Court has decided a mining lease is more than a sale and delivery of property, in that it involves a manufacturing process, and that royalties are income of the business and as such subject to taxation. It concludes Congress intended to tax said proceeds—called royalties in its opinion—after deduction therefrom of a reasonable allowance for depletion.

Such declaration of the lower Court is erroneous in at least three aspects.

First, What this Court may have decided about a mining lease is not decisive where a mining property is sold, and no property interest is retained.

Second, Loosely terming the sale proceeds as royalties, omits their meaning.

In *Ferguson* v. *Commissioner,* 45 Fed. (2d) 573, (C. C. A. 5), another case of sale of mineral in place, involving the propriety of statutory depletion either against a seven-eighths interest sold in place, or against the remaining one-eighth interest receivable when produced as the sale consideration, or against both, it is said:

> "Royalties represent the retained interest of the lessor or the vendor in the property or minerals which he receives from time to time as revenues under the contract. He (Ferguson) did not convey that interest under the deed or lease, but provided that he should receive a fraction of the minerals themselves."

The real meaning of the receipts herein as proceeds of a sale, and not as royalties from any interest retained in the property, was further available to the

lower court by reference to and recognition of the similar situation, excepting the provision therein for additional payment of the value of part of the mineral produced, described by this Court in *Group No. One Oil Corporation* v. *Bass,* 283 U. S. 279, 281, another case of sale in place, as follows:

> "*The leases conveyed all the oil and gas* in granting the right to find, produce, and appropriate all of them, *in consideration of the payment of stipulated sums and also the value of a stated fraction of the oil and gas produced.*" (Italics supplied.)

When the typical contract herein granted the operator "*the sole and exclusive privilege of mining and coking coal*" it likewise (paraphrasing the above quotation) "*conveyed all the coal in granting the right to find, produce, and appropriate all,*" as said by this Court, and there was no retained interest.

Third, and lastly, the vendor, or assignee, thereby never got into the mining business nor became interested in its manufacturing processes, for, since 1901 or 1902, the vendor owned neither coal nor interest therein, and petitioner Company has never owned any coal or interest in coal.

The conclusion of the lower court that Congress intended to tax said proceeds after allowing depletion deductions, considered alone, is equally without foundation.

In the first place, Congress could not tax the proceeds of the capital claim for reasons previously given. To do so violates the constitutional provisions which

limit the power of Congress to tax income and no more, under the Sixteenth Amendment.

This Court said in *Nichols* v. *Coolidge,* 274 U. S. 531, 541:

> * * * "under the mere guise of reaching something within its powers, Congress may not lay a charge upon what is beyond them. Taxes are very real things and statutes imposing them are estimated by practical results."

In the second place, a sale in place being a severance of the estate of the grantor, such grantor is not a lessor, and, as depletion is allowed by Congress only upon the taxpayer's interest in the mine, the grantor has no depletable interest after the sale in place was effected.

A sale of mineral in place effects a complete severance of the estate conveyed (*Group No. One Oil Corporation* v. *Bass,* 283 U. S. 279), wherein certain alleged immunities of a grantor were declared severed lost to its grantee by a sale in place, as distinguished from their preservation and benefit to a lessee, under the same contract in a state not recognizing the rule of sale in place, in the later decision of *Burnet* v. *Coronado Oil and Gas Co.,* 285 U. S. 393. The payments by the vendee for coal bought in place are capital expenditures and not the deductible rentals of a lessee (*Jefferson Gas Coal Co. v. Commissioner,* 52 F. (2) 120 (C. C. A. 3)).

The Congress in the Revenue Acts provides for allowance of depletion deductions only to the owner, or to the lessor and lessee of a mine (Cf. Statutes quoted in Appendix), saying:

> "* * * That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (*or the taxpayer's interest therein*) on that date shall be taken in lieu of cost up to that date. (Section 234(*g*), R. A. of 1918.)"

Hence, Congress allows no depletion to a vendor, or his assignee, after sale of his interest in the property. The depletion deduction is not a matter of right, and express authority therefor must be found in the Revenue Acts (*Stanton* v. *Baltic M. Co.*, 240 U. S. 103; *Burnet* v. *Thompson Oil and Gas Co.*, 283 U. S. 301). The essential statutory test, either for depletion or depreciation is the interest of the claimant in the property for as said of a statutory deduction for depreciation, in *Weiss* v. *Wiener*, 279 U. S. 333, 336:

> —"he must show an interest in the property and a present loss to make the statute apply."

In *Murphy Oil Co.* v. *Burnet*, 55 F. (2d) 17 (C. C. A. 9), we read:

> "The statute, with reference to depletion * * * is a special one * * * involving the production of oil and minerals from mines, and *the consequent return of capital by the owners of interests therein*, and controls over other general provisions of the law in regard to the return of capital investment." (Italics supplied.)

In *Darby Lynde Co.* v. *Commissioner*, 51 F. (2d) 32 (C. C. A. 10) (Cert. denied 52 S. C. 40), a discovery value available to a partnership as a basis of depletion

under the statute is denied to a successor corporation created and owned by the partners. In *Pugh* v. *Commissioner*, 49 F. (2d) 76 (C. C. A. 5) (Cert. denied, 52 S. C. 22), a taxpayer is held to have lost his right to depletion of his lease interest after conveyance of such interest because he thereby became a lessee without investment. In *South Vernon Oil Co.* v. *Hopkins*, 49 F. (2d) 1028 (C. C. A. 5), we have the same conclusion and the reason stated that the sale severed the depletable interest in the property.

Third, in case of a severance of interest, of a sale, the Congress has in the Revenue Acts made other provisions, entirely apart from depletion, for taxing any capital gain. Thus, in Texas, where, as in West Virginia, the State rule of sale of mineral in place governs such matters, a taxpayer leased seven-eighths of the mineral, while retaining the other one-eighth interest, and received a cash bonus and royalties. That he thus sold the seven-eighths interest in place, making his bonus receipt subject to the special tax rate upon a capital gain, and that only his retained interest remained subject to depletion is the decision in *Ferguson* v. *Commissioner*, 45 F. (2d) 573 (C. C. A. 5). In *Harmel* v. *Commissioner*, 56 F. (2d) 153 (C. C. A. 5), the same conclusion is reached upon authority of *Group No. One Oil Corporation* v. *Bass*, and other decisions of this Court. In *Alexander* v. *King*, 46 F. (2d) 235, in a very similar case, the capital gain provision is held inapplicable because the Oklahoma rule of property does not recognize a sale of mineral in place and ascertains the parties to be lessor and lessee. (Cf. *Burnet* v. *Coronado Oil and Gas Co.*, 285 U. S. 393 (*supra*).)

Lastly, the ruling of the lower court herein is not logical in results. If notwithstanding a sale in place, the vendor is held entitled to depletion, although he has parted with the property, this conflicts with the established rule that depletion is incident to the property interest. It deprives the vendee, as the sole owner of the property, of some part of its depletion deduction, and converts his capital payments of installments of the purchase money into rentals in the hands of the recipient. It creates an allowance not authorized by law.

The lower court (R., p. 124), after finding petitioner Company stands in the shoes of a grantor and not of a lessor as the result of the sale in place, nevertheless decides that petitioner is a lessor to which the subsequent payments are income, buttressing this decision (R., p. 124) with the statement:

> "The Federal courts must respect the local laws of property laid down by the courts of the State, but the power of Congress to tax must be judged by the realities of the situation and not by the logic of State rules of property, pushed inexorably to their extreme."

We would point out wherein this Court disapproves this statement.

Such opinion conclusion flows from discussion of earlier decisions of this Court (*Stanton* v. *Baltic Mining Co.*, 240 U. S. 103; *Strattons Independence* v. *Howbert*, 231 U. S. 399; *Von Baumbach* v. *Sargent Land Co.*, 242 U. S. 503), with special emphasis upon cases in which certiorari was denied (R., p. 123) (*Rosen-*

berger v. *McCaughn*, 25 F. (2d) 699; *Hirschi* v. *United States*, 67 Ct. Cl. 637; *Berg* v. *Commissioner*, 33 F. (2d) 641; *Burkett* v. *Commissioner*, 31 F. (2d) 667; *Alexander* v. *King*, 46 F. (2d) 235), and the statement (R., p. 125), that later decisions of this Court (*Tyler, Admr.*, v. *United States*, 281 U. S. 497; *Crooks* v. *Harrelson*, 282 U. S. 55; *Poe* v. *Seaborn*, 282 U. S. 101, omitting *Group No. One Oil Corp.* v. *Bass*, 283 U. S. 279), are not progressive to acceptance of the State rule of property in determining the liability to tax, because (R., p. 125);

> "It is obvious that each of these decisions turned upon the fundamental question whether the property sought to be taxed came within the purview of the taxing statutes."

However, such precise fundamental question is the gravamen of this case, and the lower court—like the Board in its decision of this case—labors in a former twilight of tax decisions, now lifted by this Court. Such zone of error has arisen by acceptance of denials of certiorari as being a contradiction or modification of previous decisions of this Court; notwithstanding, this Court has repeatedly declared a denial of certiorari does not have such effect (*United States* v. *Carver*, 260 U. S. 482; *Atlantic C. L. Co.* v. *Powe*, 283 U. S. 401), and expresses no opinion upon the merits of said cases.

In other words, a supposed Federal rule of property, instead of the State rule of property, was reared by the Board as decisive herein of the taxability of the purchase money payments, and previously such

supposed Federal rule affected the decision of the Circuit Judge in the West Virginia litigation of petitioner Company (R., p. 50). The lower Court restates and relies upon such Federal rule herein as being established by numerous denials of certiorari (R., p. 123). The announcement of said Federal rule, as in disregard of the State rule of property, made in May, 1929, in *Hirschi* v. *United States*, 67 Ct. Cl. 637 (Cert. denied, 280 U. S. 576), holding a sale of mineral in place under the Texas property rule is not given effect under the Federal tax laws, is quoted (R., p. 51) in the Board opinion as follows:

> "The Federal Government is not limited in its selection of subjects for taxation by the construction of the State courts as to the property rights of individuals, provided the subject taxed was primarily a proper subject for taxation. *Congress in passing a revenue act does not, and is not called upon to suit the revenue system of the country to the varying and conflicting decisions and laws of the different States.*" (Italics supplied.)

This Federal rule of property found support in *Berg v. Commissioner*, 33 F. (2d) 641 (Cert. denied, 280 U. S. 598), decided in June, 1929, and in the earlier decision of *Rosenberger* v. *McCaughn*, 25 F. (2d) 699, (C. C. A. 3) (Cert. denied, 278 U. S. 604). The Board decision in January, 1930, and its affirmance by the lower Court in January, 1932, are thus but additional expressions of such rule.

We may say each precedent relied upon by the Board had previously become final, and the Federal rule

seemed established, but that this Court had repudiated the rule before the lower Court adopted and reaffirmed the rule.

After the Board decision, in November, 1930, this Court definitely struck the rule down in *Poe, Collector* v. *Seaborn,* 282 U. S. 101, 117, saying:

> "Finally, the argument is pressed upon us that the Commissioner's ruling will work uniformity of incidence and operation of the tax in the various States, while the view urged by the taxpayer will make the tax fall unevenly on married people. * * * The answer to such argument, however, is that the constitutional requirement of uniformity is not intrinsic, but geographic. *Billings* v. *United States,* 232 U. S. 261; *Head Money Cases,* 112 U. S. 580; *Knowlton* v. *Moore,* 178 U. S. 41. And differences of State law, which may bring a person within or without the category designated by Congress as taxable may not be read into the Revenue Act to spell out a lack of uniformity. *Florida* v. *Mellon,* 273 U. S. 12."

Again, this Court struck the Federal rule down, and relied upon the State rule, in the income tax of *Phillips v. Commissioner,* 283 U. S. 589, decided in May, 1931. The State rule of sale in place found full effect in April, 1931, in the income tax case, *Group No. One Oil Corp.* v. *Bass,* 283 U. S. 279. The State rule of property, in the excise tax cases of *Tyler* v. *United States,* 281 U. S. 497, decided in May, 1930, and in *Crooks* v. *Harrelson,* 282 U. S. 55, decided in November, 1930, is upheld.

Thus, any zone of error and uncertainty existing when the Board decided these cases in January, 1930, was removed by decisions of this Court before the lower Court rendered its opinion in January, 1932.

In its decision of *Crooks* v. *Harrelson* (*supra*), this Court (p. 63), expressly disapproved *Steedman* v. *United States*, 63 Ct. Cl. 226 (Cert. denied 275 U. S. 528), upon which the Hirschi decision is substantially rested by the Court of Claims.

Federal observance of the State rules of property if the ownership of property is to be determined, springs from early decisions of this Court (*McCormick* v. *Sullivant*, 10 Wheat. 192, 202; *United States* v. *Fox*, 4 Otto 315), and is precisely reflected in later decisions under the Revenue Acts (*Poe* v. *Seaborn*, 282 U. S. 101; *Group No. One Oil Corp.* v. *Bass*, *supra*).

Only two cases, as the result of denials of certiorari, stand in the way of the uniform application of the State rule of property in cases of sales of mineral in place. They are *Hirschi* v. *United States*, 67 Ct. Cl. 637 (Cert. denied 280 U. S. 576), and *Rosenberger* v. *McCaughn*, 25 F. (2d) 699 (C. C. A. 3) (Certiorari denied 278 U. S. 604).

In *Crooks* v. *Harrelson*, this Court has expressly disapproved *Steedman* v. *United States*, 63 Ct. Cl. 226 (Cert. denied 275 U. S. 528), upon which the Court of Claims substantially rested the Hirschi decision.

Hirschi v. *United States* and *Rosenberger* v. *McCaughn*, are now in effect disapproved by *Group No. One Oil Corp.* v. *Bass* as decided in this Court.

The conclusion of *Rosenberger* v. *McCaughn* reaffirmed by the lower Court herein:

> "that the rules of decision laid down by the State courts with regard to property, while, generally controlling upon the Federal courts, do not necessarily govern those courts in the interpretation of the laws of Congress"—,

as derived from earlier tax decisions of this Court requires some explanation. It rests upon a review by the lower Court of earlier decisions of this Court, and which decisions, we submit, are inapplicable to the present case.

Strattons Independence v. Howbert, 231 U. S. 399, arose before the Sixteenth Amendment, and decided the Excise Tax of 1909, upon the conduct of a business in a corporate capacity, which measured the tax by the corporate income, was applicable to corporate gains from operating mines as derived from a business of "transmitting a part of the realty into personalty and putting it into marketable form."

Von Baumbach v. *Sargent Land Co.,* 242 U. S. 503, involved the same Excise Tax of 1909. It was held the taxpayer was a corporate lessor under the laws of Minnesota, receiving payments which were:

> "not in substance the proceeds of an outright sale of mining property, but, in view of the terms of these instruments were in fact rents or royalties * * * within the term 'income' as intended to be reached and taxed under the terms of the Corporation Tax Act,"

was not entitled to any depletion thereon, and that it was unnecessary to determine whether the established law of the State should be followed in considering the Corporation Tax Act.

Stanton v. *Baltic Mining Co.*, 240 U. S. 103, decided that pursuant to the Sixteenth Amendment an income tax upon income of a corporation derived from mining operations upon its own lands is essentially the same as the income tax imposed upon corporations engaged in other business.

United States v. *Biwabik Mining Co.*, 247 U. S. 116, again involved the Excise Tax of 1909, and decided a corporate lessee, upon authority of the Von Baumbach case, is in no sense a purchaser of ore in place, and is not entitled to any depletion.

Lynch v. *Allworth Stevens Co.*, 267 U. S. 364, involved the Revenue Act of 1916 and held the lessor and lessee each had a depletable interest in mineral being mined, which was deductible from gross income under a provision of said Act authorizing the deduction to compensate for property exhaustion.

The *Baltic Mining Company* decision must be read in connection with *Brushaber* v. *Union Pacific R. Co.*, 240 U. S. 1, in considering its statement that:

> "independently of the effect on the operation of the Sixteenth Amendment, it was settled in *Strattons Independence* v. *Howbert* that such tax is not a tax upon property as such because of its ownership, but a true excise levied on the results of the business of carrying on mining operations."

In the *Brushaber* case (pp. 16, 17) we read:

> "* * * The conclusion reached in the *Pollock* case did not in any degree involve holding that income taxes generally and necessarily came within the class of direct taxes upon prop-

> erty, but, on the contrary, recognized the fact that taxation on income was in its nature an excise entitled to be enforced as such unless and until it was concluded that to enforce it would amount to accomplishing the result which the requirement as to apportionment of direct taxation was adopted to prevent, in which case the duty would arise to disregard form and consider substance alone, and hence subject the tax to the regulation as to apportionment which otherwise as an excise would not apply to it. * * *"

This conception of income tax has been clarified in *Bromley* v. *McCaughn*, 280 U. S. 124, 136, as follows:

> "While taxes levied upon and collected from persons because of their general ownership of property may be taken to be direct (*Pollock* case, 157 U. S. 429), this Court has consistently held, almost from the foundation of the Government, that a tax imposed upon a particular use of property, or the exercise of a single power over property incidental to ownership is an excise which need not be apportioned, * * *."

Now, herein petitioner Company never owned any coal nor any interest in same, and is not within any of the cases cited in that respect. Petitioner Company has never been in the mining business; its predecessor sold the coal which thereby became and is the property of the operating company, whose income therefrom is taxable under the rule of the *Baltic Mining Company* case. Petitioner Company is not an owner of coal, nor a lessor thereof, and its receipts are not derived from

"transmitting * * * realty into personalty" as said in *Stratton's Independence* v. *Howbert.* Said income flows from purchase money, the proceeds of a sale in place, the result of a severance of interest—represented by ownership of the right to collect said sale proceeds when subsequently paid.

If the income tax upon all corporations is *"a true excise on the business of carrying on —— operations"* (quoting from the *Baltic Mining Company* opinion and deleting *"mining"*), there must be some point of severance. Otherwise, the vendor of land within which coal or oil is subsequently discovered, is thereby put in the mining business through the mere subsequent collection of the purchase price although he may not of right require the property to be mined nor control its use in any way.

In *Stratton's Independence,* this Court indicates the limit of the doctrine by saying:

> "The sale outright of a mining property might fairly be described as a mere conversion of the capital from land into money."

Such outright sale being here admitted, and transfer of ownership being thereby obtained and a conversion of property being effected, the relation of the income tax to the new asset—to the contract right to the proceeds of sale—is the remaining question.

Therefore, all attempt to consider the vendor or his assignee in the mining business by reference to the foregoing decisions of this Court is without application.

The Revenue Acts lay a tax upon the net income of every corporation, and, speaking of the identical provision in the case of individuals, this Court says, in *Poe, Collector,* v. *Seaborn,* 282 U. S. 101, 109:

> "The Act goes no farther, and furnishes no other standard or definition of what constitutes an individual's income. The use of the word 'of' denotes ownership. It would be a strained construction, which, in the absence of a further defintion by Congress, should impute a broader significance to in the term.
>
> "The Commissioner concedes that the answer to the question involved in the cause must be found in the provisions of the law of the State, as to a wife's ownership of interest in community property."

In other words, given the case where a sale of mineral in place has occurred under the State law, no interest in mining or its business can be attributed to the vendor or his assignor in the present case, and there is no depletable interest. The error of the rulings of the lower Court to the contrary are thus apparent and material.

If petitioner Company is entitled to the statutory depletion allowances of a lessor, same apply to the excess of minimum payments each year over payments for coal actually mined in each year, and the entirety of such excess is not taxable income.

The Board held, and the lower court affirmed its decision, that the excess of annual payments over

annual payments therein for coal actually mined, being a bonus payment, was taxable income not subject to the depletion allowances of a lessor. In presenting a redetermination of tax based on this ruling, the Commissioner, by counsel, voiced disagreement therewith, and stood with petitioners, contending depletion should be allowed against said excess payments. Contemporaneously therewith, the Commissioner, by cross-appeal in *Murphy Oil Co.* v. *Commissioner*, 55 F. (2d) 17 (C. C. A. 9), sought to and did sustain his position that the Board was wrong in so holding in the case of a lessee. The wrong to a lessee so established adjudges existence of the same error of omission in the case of the alleged lessor herein.

The materiality of the error is threefold: *First*, The special statutory provision allowing depletion to the owners of interests in mining property reasonably applies to all payments made for any interest in said property, where bonus, excess of minimum, or usual payment per ton mined. *Second*—The present value of the typical contract, or all the contracts herein, rests upon giving effect to the minimum payment; the Commissioner rests the 3.6 cent allowance per ton upon assumption of 14,000,000 tons minable at 350,000 tons per year, indicating a useful life of 40 years with annual income of $34,000. After 40 years, the receipts equal $1,360,000, of which the present worth on March 1, 1913, is $510,000, and this divided by 14,000,000 tons, gives 3.6 cents per ton. Allowance of this amount only upon tonnage mined is improper in that, for example,

if $34,000 is received in a taxable year but only $17,000 of coal is mined, then an additional $17,000 is received without depletion. Thus petitioner Company is really allowed 1.8 cents instead of 3.6 cents, in the example, upon the $34,000 payment which entered into the computation of the 3.6 cent unit rate. If $68,000 is received and $17,000 is mined, petitioner Company has a 0.9 cent rate instead of 3.6 cents. *Third*—If petitioner Company receives $200 as a 10 cent payment per ton on 2,000 tons, but only 1,000 tons were mined the decision below says its depletion is 1,000 x 3.6 cents, or $36.00, and is not 2,000 x 3.6 cents, or $72.00. The schedules in the Board findings as to Leases 2 and 4 (Petition for Reargument, R., p. 160), show in the seven years here in controversy, petitioner Company is deprived of $72,000 of depletion upon an excess of 2,000,000 tons paid for but not mined, and is required to taxpay said amount.

Article 216, Regulations 69 (appendix), presents the proper and reasonable method of computing and applying the deduction, as said in *Murphy Oil Co., supra:*

> * * * "by assuming that the bonus contains the same element of profit of income to the landlord that would be derived from the sale of oil recovered as royalty."
>
> "The regulation is not only not in conflict with the statute, but directly conforms thereto."

By narrow interpretation it might well be said no question of bonus is adequately present in these cases, for Article 216 contemplates "a bonus in addition to

royalties", while herein the "royalties" are dubbed "bonus" when they exceed the payments for coal mined. As the royalties enter into the computation of the depletion allowance, such allowance reasonably is deductible from all subsequent royalty receipts whether all the coal thereby paid for is mined in the year of payment.

Petitioners urge that the Board decision and its blanket affirmance by the lower Court are in error, that the Commissioner gave effect to the proper computation in Article 216 (*supra*) and obtained approval thereof in *Murphy Oil Co.* v. *Commissioner, supra,* and that, if pertinent, the depletion allowance herein should be so computed, and the lower Court reversed.

The res adjudicata herein against the Commissioner, upon the depletion issue, of a judgment involving said issue and obtained by petitioner Company in a prior action against a Collector, whom therein the Commissioner defended of record.

Before the Board, petitioner Company pleaded the District Court judgment obtained against the Collector and paid by the United States as *res adjudicata* herein of any depletion rate allowable to a lessor in its position, and the Commissioner did not answer. The Board received the record and judgment in evidence as merely persuasive and not conclusive (R., p. 103), to which ruling petitioner Company excepted, It appeared no changes or alterations in the original sale contracts, and no new contracts, had been made since the institution of the prior litigation (R., p. 101).

The Board made finding of fact as to the nature and result of the prior litigation (R., p. 47), but its opinion states no conclusion thereon. The lower Court, reviewing the facts, held the West Virginia judgment was not *res adjudicata* against the Commissioner of Internal Revenue (R., p. 126), saying:

> "The rule (*res adjudicata*) is applicable, however, only when the subsequent suit is between the same parties or their privies. The taxpayer maintains that we have that situation in the present litigation because the United States in reality is its opponent in both cases, being represented by the Collector of Internal Revenue in the prior suit, and by the Commissioner of Internal Revenue now. But the argument is refuted by the decision in *Sage* v. *United States*, 250 U. S. 33, where it was expressly ruled, against the protest of the government, that the court was not bound by a judgment in a former suit concerning the same subject matter between the taxpayer and a Collector of Internal Revenue because a suit against a collector of Internal Revenue is personal and its incidents, such as the nature of the defenses open and the allowance of interest, are different. This ruling has recently been cited with approval by the Supreme Court in *Graham & Foster* v. *Goodcell*, 282 U. S. 409, 430. The decision of the District Court for the Southern District of West Virginia was therefore not binding upon the Commissioner, and he had the authority to determine anew, as a question of fact, what allowance should be made for the depletion of the mine."

Petitioners submit the determination of the judgment against the Collector in the prior litigation that a 5 cent depletion rate was allowable to petitioner Company is effective as a final determination of the depletion issue in these proceedings against the Commissioner of Internal Revenue from four viewpoints.

Privity of Record.—Although the action of taxpayer against collector to recover income tax is personal in its character or unique in its attributes, either the United States or the Commissioner of Internal Revenue, or both, may by their acts become bound by a judgment in favor of the taxpayer in said action.

The findings of facts herein (R., p. 47) are:

> * * * "said judgment was duly paid by the United States. In said action the Bankers Pocahontas Coal Co., one of the petitioners herein, was plaintiff; plaintiff petitioner appearing in its own right and the collector as defendant, who was defended in said action by the United States District Attorney and the Solicitor of Internal Revenue (now General Counsel). In this proceeding and in said court action the subject matter of the action and of these proceedings is the same, namely, the depletion unit allowable in computing the amount of such depletion deduction as will return to the taxpayer the capital value existing in the coal content of the corporation's property as of March 1, 1913."

The official appearance of the Solicitor of Internal Revenue who is counsel for the Commissioner of Internal Revenue, renders said Commissioner privy to said proceeding and bound by the ensuing judgment

under the rule stated in *Souffront v. LaCompagnie*, 217 U. S. 475, 487, as follows:

> "*The persons for whose benefit, to the knowledge of the court and of all the parties to the record, litigation is being conducted, cannot, in a legal sense, be said to be strangers to the cause.* The case is within the principle that one who prosecutes or defends a suit in the name of another to establish and protect his own right, *or who assists in the prosecution or defense of an action in aid of some interest of his own, and who does this openly, to the knowledge of the opposing party,* is as much bound by the judgment, and as fully entitled to avail himself of it, as an estoppel against an adversary party, as he would be if he had been a party to the record. *Lovejoy* v. *Murray*, 3 Wall. 1, 18 L. Ed. 129." (Italics supplied.)

To the same effect is *Beyer Co.* v. *Fleischman*, 15 F. (2d) 465 (C. C. A. 6) and the numerous authorities therein cited.

The Commissioner and the United States may ascertain the net amount recoverable in the ultimate and final judgment against the Collector by set off of tax legally due, and be concluded by the judgment. Thus, in *New York Life Insurance Co.* v. *Anderson*, 263 F. 530 (C. C. A. 2) such adjustment as made below is upheld upon authority of *Crocker* v. *Malley*, 249 U. S. 223, as an "*anamalous practice* * * * *required by federal authority*", and as "*based on a spirit of convenience*". In *Crocker* v. *Malley, supra*, decided in 1919 and cited by Mr. Justice Holmes in the *Sage* case (p. 37) opinion, he says:

"The district court, while it found for the plaintiffs, ruled that the defendant was entitled to retain out of the sum received by him the amount of the tax that they should have paid as trustees. To this the plaintiffs took a cross writ of error to the circuit court of appeals. There can be no question that, although the plaintiffs escape the larger liability, there was probable cause for the defendant's act. The Commissioner of Internal Revenue rejected the plaintiff's claim, and the statute does not leave the matter clear. The recovery, therefore, will be from the United States. Rev. Stat., Par. 989, Comp. Stat. 1916, Par. 1635. The plaintiffs, as they themselves alleged in their claim, were the persons taxed, whether they were called an association or trustees. They were taxed too much. *If the United States retains from the amount received by it the amount that it should have received, it cannot recover that sum in a subsequent suit.*" (Italics supplied.)

In *City of New Orleans* v. *Citizens Bank,* 167 U. S. 371; *Baldwin* v. *Maryland,* 179 U. S. 220, and *Gunter* v. *Atlantic C. L. R. Co.,* 200 U. S. 273, it is held that the general rule of law by which a judgment estops the parties in future litigation between them, to question either a fact or point of law necessary to the first judgment and adjudicated therein, applies to cases of taxation as well as to other subjects of litigation. In *United States* v. *Stone and Downer Co.,* 274 U. S. 225, 230, 233, 237, after recognizing said general rule, this Court says same does not apply to litigation in the Court of Customs Appeals. Very properly the same exception is available to the Board of Tax Appeals,

whereby the termination of a prior controversy there arising is not conclusive upon the same subject matter between the parties in a subsequent proceeding.

But extension of the rule in exclusion of determinations arising and obtained in the courts impinges upon and contradicts the general rule. If the "*spirit of convenience*" produces "*an anamalous practice required by federal authority*", it follows the open participation of the Commissioner in defending the Collector leaves the Commissioner bound by the results obtained and prevents him from contesting the same subject matter in later proceedings.

Official Privity.—Aside from the privity resulting from active defense of the Collector, there is sufficient official and statutory relationship to establish privity on that ground.

There is a privity of duty between the Collector and Commissioner, notwithstanding they are separate officers, appointed by the President (R. S. 319, 3142); the Commissioner has general charge of the assessment and collection of taxes (R. S. 321), remits, refunds and pays back taxes illegally or erroneously collected, and repays the Collector adjudged tax recoveries with the costs and expenses of suit (R. S. 3220); his discretion is not reviewable by any other officer of the Government (*Kaufman's* case, 96 U. S. 568) and he may satisfy a judgment against a Collector without issue of a certificate of probable cause (*United States* v. *Frerichs,* 124 U. S. 315; the Collector gives bond in the amount prescribed by the Commissioner (R. S. 3143), sues for the recovery of taxes in the name of the United States when authorized to do so by the Com-

missioner (R. S. 3213, 3214). A taxpayer may not sue a Collector to recover taxes except after previous presentation of his claim to the Commissioner (R. S. 3226). Thus both are intimately related in their official duties, the Collector being substantially the agent of the Commissioner.

No Immunity to Commissioner.—The pertinent Revenue Acts merely provide that where the Commissioner determines a deficiency of tax "the taxpayer may file a petition with the Board of Tax Appeals for redetermination of the deficiency" (Rev. Act of 1926, 274(*a*)). This Court said in *Blair* v. *Oesterlein Mach. Co.*, 275 U. S. 220, 227 of the Board's ensuing authority:

> "It may investigate anew the issues between the government and the taxpayer and upon the determination of the appeal it may affirm, set aside or modify the findings and decision of the Commissioner."

This Court has further said the decision of the Board may be reviewed in the Circuit Courts of Appeals and herein (*Old Colony Trust Co.* v. *Commissioner*, 279 U. S. 716, 721).

Thus the Revenue Acts afford taxpayer another remedy, in addition to the taxpayer's right of action after payment of a Federal tax for recovery of same previously existing against either the Collector of Internal Revenue or the United States. It does not follow there is any immunity to the Commissioner of Internal Revenue.

Any immunity of the sovereign claimed by its agent must be established by production of a law, which com-

missions the party claiming the immunity and warrants the act sought to be avoided (*Poindexter* v. *Greenhow,* 114 U. S. 270, 288), but no such law is produced herein, for none exists.

In the *Poindexter* opinion, *supra* (p. 288), we read:

> "The *ratio decidendi* in this class of cases is very plain. A defendant sued as a wrongdoer, who seeks to substitute the state in his place, or to defend on the ground that the state has adopted his act and exonerated him, cannot rest on the bare assertion of his defense. He is bound to establish it. The state is a political corporate body, can act only through agents, and can command only by laws. It is necessary, therefore, for such a defendant, in order to complete his defense, to produce a law of the state which constitutes his commission as its agent, and a warrant for his act."

The Commissioner, as respondent before the Board as in subsequent proceedings, cannot invoke the immunity of the United States (*United States* v. *Lee,* 106 U. S. 196; *Trudal* v. *Wesley,* 167 U. S. 204, 222; *Scranton* v. *Wheeler,* 179 U. S. 141, 153).

No Immunity to the United States.—This viewpoint has reference to the effect of the proceedings mentioned in the *Sage* case as subsequent to the judgment, whereby, upon issue by the trial court of the certificate of probable cause under R. S. 989, payment of the judgment is made by the United States. The effect of the issue of the certificate of probable cause is declared in *United States* v. *Sherman,* 98 U. S. 565, 567.

> "When the certificate is given the claim of the plaintiff in the suit is practically converted

> into a claim against the government. But not until then."

The final judgment contemplated by R. S. 989 is defined in *Schell* v. *Cochran*, 107 U. S. 625, with approval therein of the *Sherman* decision.

A claim against the Government, which it subsequently has paid, being so established by statutory authority, it reasonably follows that the Government had adopted the judgment in all its implications and findings, and is bound by same. This recognizes the principle that the Government may not be sued without its consent (*Carr* v. *United States*, 98 U. S. 433), and yet gives effect either to R. S. 989 wherein the Government authorizes the trial court to impose the individual liability of its officer upon the Government, or to R. S. 3220, whereby the Commissioner makes the judgment binding upon the Government by an award thereon to the taxpayer without previous issue of the certificate of probable cause (*United States* v. *Frerichs*, 124 U. S. 315, 319). Said effect is declared in *N. Y. C. & H. R. R. Co.* v. *United States*, 24 Ct. Cl. 22, 29:

> "It is impossible to suppose that the law intends to allow an action to be prosecuted against a public officer, an appeal to be taken, a defense to be maintained by the Government through its proper law officers, a judgment to be recovered under the direction of our highest judicial authority, and the right thus acquired to be immediately taken away by a certificate resting upon the discretion of a single judge, upon an issue not tried by a jury, and allowed by an order from which there is no appeal, unless it

> likewise intends that the absolute discharge of the agent shall operate as an assumption of the debt by the principal."

In other words, the Government upon issue of the certificate of probable cause takes over and assumes the obligations of the agent, whereby the conclusive effect of the judgment may become available to the taxpayer in subsequent litigation on the same subject matter under the theory of *Crocker* v. *Malley, supra.* It does not appear whether this aspect was presented in the *Sage* case, except the opinion almost reaches the proposition and turns abruptly to the facts in that case, to say:

> "But perhaps it would be enough to say that if the judgment otherwise were a bar, the bar would be removed by the subsequent enactment of the Act of July 27, 1912, upon which, as well as upon the Act of 1902, this claim is based."

In *Second National Bank of Saginaw* v. *Woodworth, Collector,* 54 F. (2) 672, an action of taxpayer brought against the United States for recovery of taxes in the Court of Claims being ordered dismissed, the Collector is held entitled to rely on said order as an estoppel and *res adjudicata.* The decision is rested upon the test of privity whereby, unless the Collector may so defend, the United States might through a certificate of probable cause be obligated for a demand previously litigated and defeated in an action against the Government. But the alleged privity herein leads to no such illogical situation, whereas it is equally illogical that although the Government may not by indirection be

made liable for a claim it has previously defeated, the taxpayer may be made liable for a claim which it has previously defeated.

The finality of Board proceedings after judicial review thereof as declared by the Revenue Act of 1926, *Section 283(b)*, is held available to a Collector in *Greylock Mills* v. *White*, 55 F. (2) 704, and the finality of a judgment adopted and satisfied under a statutory certificate of probable cause should be equally available to the taxpayer in a subsequent controversy with the Commissioner as to the same subject matter.

For these reasons, the refusal of the lower Court to give effect herein, if applicable, to the depletion rate previously adjudged in litigation against the Collector is presented as error.

The Strother Relief.

It was stipulated below that the decision of the case of petitioner Company should adjudicate the case of petitioner Strother. The lower Court directed supplemental proceedings before the Board should be had to ascertain his possible tax liability. The propriety of the relief so granted is not open to challenge herein because the Commissioner of Internal Revenue neither applied for nor obtained a writ of certiorari in reference thereto. *Lucas* v. *Alexander*, 279 U. S. 573.

Conclusion.

It is respectfully submitted the lower Court should be reversed herein for cause:

That it erred in refusing to hold the contract proceeds from the sale in place received by petitioner

Company were not taxable income in the years in controversy.

That it erred in holding Congress intended by the Revenue Acts to tax same as the receipts of a lessor.

That it erred, if it appear in the alternative said proceeds are taxable as receipts of a lessor, in neither allowing a rate of 5 cents per ton adjudicated to petitioner Company in prior litigation, nor in allowing depletion upon payments in excess of coal actually mined and paid for in the taxable periods.

And petitioners abide the decision of the Court.

Respectfully,

WELLS GOODYKOONTZ,
CAMDEN R. McATEE,
Attorneys for Petitioners.

GOODYKOONTZ AND SLAVEN,
Williamson, West Virginia,
MASON, SPALDING & McATEE,
Washington, D. C.,
Of Counsel.

APPENDIX.

Constitution, Statutes and Regulations Involved.

The Constitution of the United States.

Amendment Sixteen (effective March 1, 1913). The Congress shall have power to lay and collect taxes on incomes from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

Individual Gross Income.

Revenue Act of 1918, Section 213 (40 Stat. 1057-96, C. 18):

> "That for the purposes of this title (except as otherwise provided in section 233) the term 'gross income'—
>
> "(*a*) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever."

Revenue Act of 1921, Section 213 (same as above). (42 Stat. 227, C. 136.)

Revenue Act of 1924, Section 213 (same as Revenue Act of 1918 above). (43 Stat. 253, C. 234.)

Revenue Act of 1926, Section 213 (same as Revenue Act of 1918 above). (44 Stat. (Part 2) 9, C. 27.)

Individual Net Income.

Revenue Act of 1918, Section 212 (*Idem.*):

> "That in the case of an individual the term 'net income' means the gross income as defined in section 213, less the deductions allowed by section 214."

Revenue Act of 1921, Section 212 (same as Revenue Act of 1918 above). (*Idem.*)

Revenue Act of 1924, Section 212 (same as Revenue Act of 1918 above). (*Idem.*)

Revenue Act of 1926, Section 212 (same as Revenue Act of 1918 above). (*Idem.*)

Corporation Gross Income.

Revenue Act of 1918, Section 233 (*Idem.*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'gross income' means the gross income as defined in section 213, except that:" (Exceptions not material.)

Revenue Act of 1921, Section 233 (*Idem.*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'gross income' means the gross income as defined in sections 213 and 217, * * *." (Not material here.)

Revenue Act of 1924, Section 233 (same as Revenue Act of 1921 above). (*Idem.*)

Revenue Act of 1926, Section 233 (same as Revenue Act of 1921 above). (*Idem.*)

Corporation Net Income.

Revenue Act of 1918, Section 232 (*Idem.*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233 less the deductions allowed by section 234, and the net income shall be computed on the same basis as is provided in subdivision (*b*) of section 212 or in section 226." (Omitted as relating only to accounting method.)

Revenue Act of 1921, Section 232 (*Idem.*):

> "That in the case of a corporation subject to the tax imposed by section 230 the term 'net income' means the gross income as defined in section 233, less the deductions allowed by section 234."

Revenue Act of 1924, Section 232 (same as Revenue Act of 1921 above). (*Idem.*)

Revenue Act of 1926, Section 232 (same as Revenue Act of 1921 above). (*Idem.*)

Meaning of Net Income.

Article 21 (Reg. 45, years 1918, 1919, 1920) (Reg. 62, years 1921, 1922, 1923) (Reg. 65, year 1924) (Reg. 69, years 1925, 1926):

> "The tax imposed by the statute is upon income. In the computation of the tax various classes of income must be considered:
>
> "(*a*) Income (in the broad sense), meaning all wealth which flows in to the taxpayer other than as a mere return of capital. It includes the

forms of income specifically described as gains and profits, including gains derived from the sale or other disposition of capital assets. Cash receipts alone do not always accurately reflect income, for the statute recognizes as income-determining factors other items, among which are inventories, accounts receivable, property exhaustion, and accounts payable for expenses incurred. * * *

"(*b*) Gross income, meaning income (in the broad sense) less income which is by statutory provision or otherwise exempt from the tax imposed by the statute. * * *

"(*c*) Net income, meaning gross income less statutory deductions. The statutory deductions are in general, though not exclusively, expenditures, other than capital expenditures, connected with the production of income. * * *

"(*d*) Net income less credits. * * *

"The surtax is imposed upon net income; the normal tax upon net income less credits. Although taxable net income is a statutory conception, it follows, subject to certain modifications as to exemptions and as to deductions for partial losses in some cases, the lines of commercial usage. Subject to these modifications statutory 'net income' is commercial 'net income'. This appears from the fact that ordinarily it is to be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer. As to the net income of corporations, see section 232 * * * and article 531."

Article 531 (same Regulations):

"*Net Income.*—Net income is that portion of the gross income which remains after all proper

deductions have been taken into account. The net income of corporations is determined in general in the same manner as the net income of individuals, but the deductions allowed corporations are not precisely the same as those allowed individuals. * * * The net income of corporations is to be computed on the same basis as to accounting periods as the net income of individuals."

Article 90 (same Regulations):

"*Income Accrued Prior to March 1, 1913.*—Any claim existing unconditionally on March 1, 1913, whether presently payable or not, and held by a taxpayer prior to March 1, 1913, whether evidenced by writing or not, and all interest which had accrued thereon before that date, do not constitute taxable income, although actually recovered or received subsequent to such date. Interest accruing on or after that date is taxable income. Where an interest-bearing claim held on February 28, 1913, is paid in whole or in part after that date, any gain derived from the payment of the claim is taxable. The amount of such gain is the excess of the proceeds of the claim (both principal and interest) exclusive of any interest accrued since February 28, 1913, already returned as income, over the cost thereof (both principal and interest then accrued). However, the gain to be included in gross income where the fair market value of the claim as of March 1, 1913, is greater than the cost thereof, is the excess of the amount received over such value. In the case of an insurance policy its surrender value as of March 1, 1913, may be used as a basis for

the purpose of ascertaining the gain derived from its sale or other disposition. Where services were rendered prior to March 1, 1913, but paid for thereafter, the amount received is taxable income to the extent of the excess of such amount over the fair market value on March 1, 1913, of the principal of the claim and any interest which had then accrued."

Corporation Deductions.

Revenue Act of 1918, Section 234:

"That in computing the net income of a corporation subject to the tax imposed by Section 230, there shall be allowed as deductions: * * *

"(9) In the case of mines, oil and gas wells, other natural deposits, and timber, a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost, including cost of development not otherwise deducted: *Provided,* that in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: * * * In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee."

Revenue Act of 1921, Section 234 (same as Revenue Act of 1918 above) (*Idem.*).

Revenue Act of 1924, Section 234 (same as Revenue Act of 1918 above) (*Idem.*).

Revenue Act of 1926, Section 234 (same as Revenue Act of 1918 above) (*Idem.*).

Article 204 (same Regulations as above):

"*Amount Returnable Through Depletion and Depreciation in the Case of Lessor.*—(*a*) In the case of a lessor, the amount remaining in any year returnable through depletion and depreciation deductions is (1) the value of his equity in the property at the basic date minus (2) depletion and depreciation sustained, whether legally allowable or not, from the basic date to the taxable year, plus (3) subsequent allowable capital additions, and minus (4) the value of the land at the basic date for other purposes than mineral production and the residual value of other property at the end of operations. The amount returnable through depletion is the total capital remaining less the sum recoverable through depreciation. The provisions of this paragraph do not apply to the computation of the depletion allowance in the case of oil and gas wells when such allowance is based on the income from the property.

"(*b*) The values of the equities of lessor and lessee shall be computed separately, but, when determined as of the same basic date, shall together never exceed the value at that date of the property in fee simple. * * *

"(*d*) The value of the lessor's equity in a mineral property under lease March 1, 1913, for the entire operating life of the mineral deposits is to be taken to mean (1) the cost or (2) the value as of March 1, 1913, of the royalties and other payments to be expected under the terms of the lease in effect on that date, whichever is greater."

Article 215 (Regulations 45, 62, 65 above):

"*Depletion-Adjustments of Accounts on Bonus or Advanced Royalties.*—(*a*) Where a

lessor receives a bonus or other sum in addition to royalties, such bonus or other sum shall be regarded as a return of capital to the lessor, but only to the extent of the capital remaining to be recovered through depletion by the lessor at the date of lease. If the bonus exceeds the capital remaining to be recovered, the excess and all the royalties thereafter received will be income and not depletable. If the bonus is less than the capital remaining to be recovered by the lessor through depletion, the difference may be recovered through depletion deductions based on the royalties thereafter received. The bonus or other sum paid by the lessee for a lease made on or after March 1, 1913, will be his value for depletion as of date of acquisition."

Article 216 (215) (Regulations 69 above amending Article 215):

"*Depletion-Adjustments of Accounts Based on Bonus or Advanced Royalty.*—(*a*) Where a lessor receives a bonus in addition to royalties, there shall be allowed as a depletion deduction in respect of the bonus an amount equal to that proportion of the cost or value of the property on the basic date which the amount of the bonus bears to the sum of the bonus and the royalties expected to be received. Such allowance shall be deducted from the amount remaining to be recovered by the lessor through depletion, and the remainder is recoverable through depletion deductions on the basis of royalties thereafter received."

Dividends.

Revenue Act of 1918, Section 201 (*Idem.*):

"(*a*) That the term 'dividend' when used in this title (except in paragraph (10) of subdivision (*a*) of section 234) means (1) any distribution made by a corporation, other than a personal service corporation, to its shareholders or members, whether in cash or in other property or in stock of the corporation, out of its earnings or profits accumulated since February 28, 1913 * * *.

"(*b*) Any distribution shall be deemed to have been made from earnings or profits unless all earnings and profits have first been distributed. * * *

"(*c*) Any distribution made during the first sixty days of any taxable year shall be deemed to have been made from earnings or profits accumulated during preceding taxable years; but any distribution made during the remainder of the taxable year shall be deemed to have been made from earnings or profits accumulated between the close of the preceding taxable year and the date of distribution, to the extent of such earnings or profits, and if the books of the corporation do not show the amount of such earnings or profits, the earnings or profits for the accounting period within which the distribution was made shall be deemed to have been accumulated ratably during such period."

Revenue Act of 1921, Section 201 (*Idem.*):

"(*a*) That the term 'dividend' when used in this title (except in paragraph (10) of subdivi-

sion (*a*) of section 234 and paragraph (4) of subdivision (*a*) of section 245) means any distribution made by a corporation to its shareholders or members, whether in cash or in other property, out of its earnings or profits accumulated since February 28, 1913. * * *

"(*b*) For the purposes of this Act every distribution is made out of earnings or profits, and from the most recently accumulated earnings or profits, to the extent of such earnings or profits accumulated since February 28, 1913; but any earnings or profits accumulated or increase in value of property accrued prior to March 1, 1913, may be distributed exempt from the tax, after the earnings and profits accumulated since February 28, 1913, have been distributed. * * *

"(*f*) Any distribution made during the first sixty days of any taxable year shall be deemed to have been made from earnings or profits accumulated during preceding taxable years; but any distribution made during the remainder of the taxable year shall be deemed to have been made from earnings or profits accumulated between the close of the preceding taxable year and the date of distribution, to the extent of such earnings and profits, and if the books of the corporation do not show the amount of such earnings or profits, the earnings or profits for the accounting period within which the distribution was made shall be deemed to have been accumulated ratably during such period. This subdivision shall not be in effect after December 31, 1921."

Revenue Act of 1924, Section 201 (same as Revenue Act of 1921 above). (*Idem.*)

Revenue Act of 1926, Section 201 (same as Revenue Act of 1921 above). (*Idem.*)

Article 1542, (Same Regulations):

> "*Source of Distribution.*—For the purpose of income taxation every distribution made by a corporation is made out of earnings or profits to the extent thereof and from the most recently accumulated earnings or profits."

Article 1543, (same Regulations):

> "*Distribution Out of Earnings or Profits Accumulated Prior to March 1, 1913.*—Any distribution by a corporation out of earnings or profits accumulated prior to March 1, 1913, or out of increase in value of property accrued prior to March 1, 1913 (whether or not realized by sale or other disposition prior to or on or after March 1, 1913) is not a dividend within the meaning of Title II. The provisions of the preceding sentence shall be applied uniformly to cases arising under the Revenue Act of 1916, the Revenue Act of 1917, the Revenue Act of 1918, the Revenue Act of 1921, and the Revenue Act of 1924, as well as the Revenue Act of 1926. A corporation cannot distribute earnings or profits accumulated or increase in value of property accrued prior to March 1, 1913, exempt from tax, unless and until all earnings or profits accumulated since February 28, 1913, have been distributed. * * *
>
> "In determining whether a dividend is out of earnings or profits accumulated since February 28, 1913, or prior to March 1, 1913, due consideration must be given to the facts, and mere bookkeeping entries increasing or decreasing surplus will not be conclusive. * * *"

Article 1546, (Same Regulations):

> "*Distributions from Depletion or Depreciation Reserves.*—A reserve set up out of gross income by a corporation and maintained for the purpose of making good any loss of capital assets on account of depletion or depreciation is not a part of surplus out of which ordinary dividends may be paid. * * * No distribution, however, can be made from such a reserve until all the earnings or profits of the corporation have first been distributed."

Certificate of Probable Cause.

R. S. 989 (12 St. L. 741, c. 76, 12):

> "When a recovery is had in any suit or proceeding against a collector or other officer of the revenue for any act done by him, or for the recovery of any money exacted by or paid to him and by him paid into the Treasury, in the performance of his official duty, and the Court certifies that there was probable cause for the act done by the collector or other officer, or that he acted under the directions of the Secretary of the Treasury, or other proper officer of the Government, no execution shall issue against such collector or other officer, but the amount so recovered shall, upon final judgment, be provided for and paid out of the proper appropriation from the Treasury."

Refunding Taxes and Penalties Including Judgments.

R. S. 3220 (14 St. L. 111, C. 184, 9; 17 St. L. 401, C. 13, 1; 40 St. L. 1145, C. 18, 1316(*a*); 44 St. L. 115, C. 27, 1111; 45 St. L. 878, C. 852, 619; 45 St. L. 996, C. 901, 3.

"Except as otherwise provided by law in the case of income, war-profits, excess-profits, estate, and gift taxes, the Commissioner of Internal Revenue, subject to regulations prescribed by the Secretary of the Treasury, is authorized to remit, refund, and pay back all taxes erroneously or illegally assessed or collected, all penalties collected without authority, and all taxes that appear to be unjustly assessed or excessive in amount, or in any manner wrongfully collected; also to repay to any collector or deputy collector the full amount of such sums of money as may be recovered against him in any court, for any internal-revenue taxes collected by him, with the cost and expense of suit; also all damages and cost recovered against any assessor, assistant assessor, collector, deputy collector, agent, or inspector, in any suit brought against him by reason of anything done in the due performance of his official duty, and shall make report to Congress, by internal-revenue districts and alphabetically arranged of all refunds in excess of $500, at the beginning of each regular session of Congress of all transactions under this section."

FILE COPY

FILED
JUL 5 1932
CHARLES ELMORE CROPLEY
CLERK

Nos. 104 and 105

In the Supreme Court of the United States

OCTOBER TERM, 1932

BANKERS POCAHONTAS COAL COMPANY, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

D. J. F. STROTHER, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

INDEX

	Page
Opinions below	1
Jurisdiction	2
Questions presented	2
Statutes and regulations involved	3
Statement	3
Argument	8
Conclusion	17
Appendix	18

CITATIONS

Cases:

Alexander v. *King*, 46 F. (2d 235, certiorari denied, 283 U. S. 845	10
Berg v. *Commissioner*, 33 F. (2d) 641, certiorari denied, 280 U. S. 598	10
Burkett v. *Commissioner*, 31 F. (2d) 667, certiorari denied, 280 U. S. 564	10
Ferguson v. *Commissioner*, 45 F. (2d) 573	11
Graham & Foster v. *Goodcell*, 282 U. S. 409	17
Harmel v. *Commissioner*, 56 F. (2d) 153, No. 26, October Term, 1932	11
Hirschi v. *United States*, 67, C. Cls. 637, certiorari denied 280 U. S. 576	10
Lynch v. *Alworth-Stephens Co.*, 267 U. S. 364	10
Murphy Oil Co. v. *Burnet*, 55 F. (2d) 17	15
Reinecke v. *Spalding*, 280 U. S. 227	12
Rosenberger v. *McCaughn*, 25 F. (2d) 699, certiorari denied 278 U. S. 604	10
Sage v. *United States*, 250 U. S. 33	16
Stanton v. *Baltic Mining Co.*, 240 U. S. 103	9
Smietanka v. *Indiana Steel Co.*, 257 U. S. 1	17
Stratton's Independence v. *Howbert*, 221 U. S. 399	9, 10
Union Trust Co. v. *Wardell*, 258 U. S. 537	17
United States v. *Biwabik Mining Co.*, 247 U. S. 116	10
United States v. *Stone & Downer*, 274 U. S. 225	17
Von Baumbach v. *Sargent Land Co.*, 242 U. S. 503	10

Statutes:	Page
Revenue Act of 1918, c. 18, Sec. 234, 40 Stat. 1057, 1077	18
Revenue Act of 1921, c. 136, Sec. 234, 42 Stat. 227, 254	18
Revenue Act of 1924, c. 234, Sec. 234, 43 Stat. 253, 283	19
Revenue Act of 1926, c. 27, Sec. 234, 44 Stat. 9, 41	19
Miscellaneous:	
T. D. 3938, C. B. V–2, pp. 117–118	22
Treasury Regulations 45, Art. 215	20, 22
Treasury Regulations 62, Art. 215	22
Treasury Regulations 65, Art. 216	22
Treasury Regulations 69, Art. 216	22, 23
Treasury Regulations 74, Art. 236	22, 23

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 104

BANKERS POCAHONTAS COAL COMPANY, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

No. 105

D. J. F. STROTHER, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 49–57)[1] is reported in 18 B. T. A. 901. The opinion of

[1] The record references refer to the record in the *Bankers Pocahontas Coal Company* case (No. 104) unless otherwise indicated.

the Circuit Court of Appeals (R. 119–134) is reported in 55 F. (2d) 626.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered in each case January 27, 1932. (R. 135–136; Strother R. 111.) A petition of the petitioners for a rehearing covering both cases was presented February 26, 1932. (R. 137–167; Strother R. 112–138.) A petition of the respondent for a rehearing in the *Strother* case was presented February 26, 1932. (Strother R. 139–141.) Both petitions were denied by an order entered March 7, 1932. (R. 169–170; Strother R. 141–142.) By leave of court, the petitioners filed a supplemental petition for rehearing on April 12, 1932. (R. 171–183; Strother R. 143–153.) The supplemental petition for rehearing was denied April 29, 1932. (R. 185; Strother R. 154.) The petition for certiorari was filed May 23, 1932. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether royalties received by the petitioner, Bankers Pocahontas Coal Company, under an instrument, in form a contract of lease, which granted the privilege of mining and coking coal on certain property in West Virginia, are taxable income.

2. Whether distributions made by that company to Strother as a stockholder were in part taxable to him as dividends.

3. Whether (in case the royalties are taxable income) an allowance for depletion should be based on the minimum royalties paid in each year or upon the number of tons actually mined, where the tonnage mined is less than the amount that the lessor had the right to mine for the minimum royalty payment.

4. Whether a judgment against a Collector of Internal Revenue in an action brought by petitioner in a United States District Court, involving other taxable years than those in question in the present case, is *res adjudicata* of certain issues in the present case.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved will be found in the Appendix, *infra,* pp. 18–23.

STATEMENT

The respondent determined deficiencies in income and profits taxes of the petitioner Bankers Pocahontas Coal Company for the years 1920 to 1926 inclusive, amounting to $39,851.99 (R. 12, 23, 29), and in income taxes of the petitioner Strother for the years 1919 to 1925, inclusive, amounting to $8,874.50. (Strother R. 11, 17, 23.) The petitioners appealed from these determinations to the Board of Tax Appeals.

The material facts as found by the Board may be summarized as follows (R. 39–49):

The petitioner Bankers Pocahontas Coal Company (hereafter called the Coal Company) is a West Virginia corporation formed in 1912. In that year it acquired in fee 6,200 acres of land in West Virginia, including the mineral rights therein. Also, by assignment, it acquired and holds the interest of the prior owners in certain contracts of lease executed in 1901 and 1902 with several coal operating companies, to which the tract of land was subject. By these contracts the prior owners did "demise, let and lease for coal mining and coal coking purposes only" to the coal operating companies severally, certain parts of the tract. The form of contract used was that prevailing in the West Virginia coal fields, and followed the form used in the State of Pennsylvania. (R. 39–40.) Extracts from a typical contract appear at R. 40–42. The cost to the Coal Company of the properties was between $407,000 and $507,000. (R. 42.)

Schedules appearing in the findings of fact (R. 43–46) contain a list of the contracts and show the estimated recoverable coal on March 1, 1913, and the number of tons mined, the number of tons paid for, and the royalty receipts in the taxable years here in question, under each contract.

In these years the Coal Company was on a cash receipts and disbursements basis of accounting. Its income, except for minor items, consisted of payments received under these contracts. (R. 46.)

The respondent treated the income as royalty payments under leases, and allowed the Coal Company, as lessor, a deduction for depletion at the rate of 3.6 cents per ton of coal mined. This is the rate that had been allowed by the respondent for 1919 and prior years. (R. 47.)

Additional taxes amounting to $6,267.08 were assessed and collected for the years 1914 to 1919, inclusive. In 1923, the Coal Company brought an action in the United States District Court for the Southern District of West Virginia against the Collector of Internal Revenue to recover those taxes. The Coal Company contended that payments received by it under the contracts were proceeds of the sale of coal in place consummated before March 1, 1913, or of choses in action owned on that date and therefore not income; or, otherwise, that in computing net income it was entitled as lessor to a depletion rate of 5 cents per ton of coal mined. The court held the receipts were income and found that the plaintiff was entitled to a depletion rate of 5 cents a ton, and entered judgment in its favor for $5,373.01, which was duly paid. The Collector of Internal Revenue, as defendant, was represented in that action by the United States Attorney and the Solicitor of Internal Revenue (now General Counsel). (R. 47.)

In the several years here involved the petitioner Strother, as a stockholder, received payments from the Coal Company. He reported them in his in-

come-tax returns but did not include them as taxable income. The Coal Company used such portion of the royalty payments as was necessary for ordinary and necessary expenses, set aside a reserve to meet pending Federal taxes, and distributed the balance to its stockholders. The respondent added the entire amount of the distribution to Strother to his net income without allowance for such part thereof as may have come out of the depletion reserve of the Coal Company. Deficiencies against Strother were determined by the respondent accordingly. (R. 72–73.)

In the case of the Coal Company, the Board of Tax Appeals held that the payments received by the petitioner under the contracts were royalties which were properly part of its gross income; that it was entitled to a reasonable allowance for depletion, and that the petitioner had failed to prove that the allowance determined by the respondent of 3.6 cents per ton was not reasonable. (R. 51, 54.) On February 27, 1930, the petitioner filed a motion for a rehearing and alleged as error, among others, that the Board had failed to hold that the decision in the case of this petitioner against the Collector of Internal Revenue, in the United States District Court for the Southern District of West Virginia, was *res adjudicata* of the issue with respect to the depletion rate. (R. 57–59.) The motion was denied. (R. 59–60.) Upon final settlement of the

amount of deficiencies under the Board's decision, petitioner filed objections to the proposed determinations submitted by respondent and presented counter proposed determinations. Petitioner therein contended for the first time that the depletion allowance should be on the basis of the minimum royalty payments and not upon the tonnage of coal mined, where the latter was less than was permitted to be mined for the minimum royalty payment in any year. (R. 66–69.) At the oral hearing on final settlement, a motion was made on behalf of both petitioners for a rehearing to enable them to offer additional evidence for the purpose of raising this question, and the Board denied the motion. (R. 69–70, 109–110.) The Board thereupon entered its order in the Coal Company case redetermining the deficiencies in the aggregate amount of $39,171.05. (R. 70–71.) The Circuit Court of Appeals sustained the decision of the Board on all of the above issues.[2]

In the Strother case, before the Board, it was agreed between the parties that the distributions received by Strother were nontaxable to the extent that they came out of the depletion reserve of the Coal Company. (R. 57.) The respondent thereupon filed a proposed settlement of the amount of

[2] There were certain other issues before the Board and the Circuit Court in the Coal Company case which are not involved in the present petition.

the deficiencies. (Strother R. 49–56.) The petitioner Strother filed objections and a counter proposal alleging error, among others, in the respondent's computation in that it did not accord with the allowances for depletion made to the Coal Company. (Strother R. 57–63, 64–70.) After oral hearing (Strother R. 81–86) the Board adopted the computations of the respondent and entered its order redetermining deficiencies aggregating $5,806.07 and an overassessment for the year 1924 to be abated in the amount of $36.38. (Strother R. 71–72.) The Circuit Court of Appeals decided Strother should be given an opportunity to introduce additional testimony on the issues raised by him on the hearing on final settlement, and it remanded this case for further proceedings in accordance with its opinion in the Coal Company case. (Strother R. 110.)

ARGUMENT

I

The Board of Tax Appeals held that the contracts in question were leases and the payments thereunder were royalties and properly part of the gross income of the Coal Company. (R. 51.) The Circuit Court of Appeals assumed for the purposes of its decision that the law of West Virginia was that a lease of coal lands constituted a sale of the coal in place, and it held that the royalty payments

nevertheless constituted taxable income. The petitioner contends, first, that the decision violates the Sixteenth Amendment to the Constitution in that it puts a tax upon the proceeds of a sale of property made prior to the effective date of the Amendment, and next, that Congress did not intend to tax such receipts.

We believe that both contentions are fully answered by previous decisions of this Court. In *Stanton* v. *Baltic Mining Co.*, 240 U. S. 103, which arose under the income-tax provisions of the Tariff Act of 1913, c. 16, 38 Stat. 166, 181, Sec. 2, it was contended that the proceeds of mining without an adequate allowance by way of deduction for exhaustion of the ore body was a tax upon property because of its ownership and therefore subject to apportionment. Of this contention, this Court said (pp. 113–114):

> It moreover rests upon the wholly fallacious assumption that looked at from the point of view of substance a tax on the product of a mine is necessarily in its essence and nature in every case a direct tax on property because of its ownership unless adequate allowance be made for the exhaustion of the ore body to result from working the mine. We say wholly fallacious assumption because independently of the effect of the operation of the Sixteenth Amendment it was settled in *Stratton's Independence* v. *How-*

bert, 231 U. S. 399, that such a tax is not a tax upon property as such because of its ownership, but a true excise levied on the results of the business of carrying on mining operations (pp. 413 *et seq.*).

That case and *Stratton's Independence* v. *Howbert*, 231 U. S. 399, involved the proceeds of ores mined by a corporation from its own premises. *Von Baumbach* v. *Sargent Land Co.*, 242 U. S. 503, involved moneys received from lessees under mining leases, and the question was whether the receipts were income under the corporation excise tax provisions of the Tariff Act of 1909, c. 6, 36 Stat. 11, 12. This Court decided, on the principles announced in the *Baltic Mining Co.* and *Stratton's Independence* cases, that the royalties received under the leases were income. It was held that since the royalties resulted from the process of mining, which is equivalent to manufacturing, the gains are "derived from capital, from labor, or from both combined." (p. 521.) See also, *United States* v. *Biwabik Mining Co.*, 247 U. S. 116; *Lynch* v. *Alworth-Stephens Co.*, 267 U. S. 364; *Hirschi* v. *United States*, 67 C. Cls. 637, certiorari denied, 280 U. S. 576; *Rosenberger* v. *McCaughn*, 25 F. (2d) 699 (C. C. A. 3d), certiorari denied, 278 U. S. 604; *Alexander* v. *King*, 46 F. (2d) 235 (C. C. A. 10th), certiorari denied, 283 U. S. 845; *Berg* v. *Commissioner*, 33 F. (2d) 641 (App. D. C.), certiorari denied, 280 U. S. 598; *Burkett* v.

Commissioner, 31 F. (2d) 667 (C. C. A. 8th), certiorari denied, 280 U. S. 565. The *Rosenberger* case, *supra,* involved the question whether royalty payments under a lease of Pennsylvania coal lands similar to the leases involved in the instant case were taxable income. The Circuit Court of Appeals held that they were, although it recognized that under Pennsylvania law such leases constituted sales of coal in place. This Court declined to review the decision.

The cases of *Ferguson* v. *Commissioner,* 45 F. (2d) 573 (C. C. A. 5th), and *Harmel* v. *Commissioner,* 56 F. (2d) 153 (C. C. A. 5th), referred to by petitioner, are not in conflict with the decision of the court below in the case at bar upon the present question. They involved the question whether bonuses or cash payments received by the lessor upon the execution of oil and gas leases of land in Texas were taxable as gain derived from the sale of a capital asset or ordinary income from the use of the property. The court held these receipts were taxable as capital gains, but in the *Ferguson* case, which also involved royalties thereafter to be received, it held that such royalties were taxable as ordinary income since they represent the retained interest of the lessor or vendor in the property or minerals, which he receives from time to time under the contract. The decision in the *Ferguson* case is therefore in accord with the case at bar so far as

the present question is concerned, and the question was not involved in the *Harmel* case.[3] Cf. *Reinecke* v. *Spalding*, 280 U. S. 227.

We submit that in any view of the legal effect of the contracts under state law the royalties received by the Coal Company were properly included in gross income.

II

Since, as we contend, the royalty payments were gross income to the Coal Company, it follows that the distributions to petitioner Strother were taxable to him as dividends to the extent that they were paid out of surplus.

---

[3] On April 18, 1932, this Court granted the Commissioner's petition for certiorari in the *Harmel* case, and it is now pending as *Burnet* v. *Harmel*, No. 26, October Term, 1932. In the *Harmel* case the court held that the Texas rule that leases of oil lands constituted sales of the oil, required the conclusion that a bonus paid upon the execution of such a lease constituted capital gain and not income. In the present case the court assumed that the leases constituted sales of the mineral in place under West Virginia law, but held, nevertheless, that royalties paid under such leases constituted taxable income. Thus as to such royalties the decision of the court below is in accord with the decision in the *Ferguson* case, so far as it concerned similar royalties. In its petition for certiorari in the *Harmel* case the Government pointed out that the decision in that case was in conflict in principle with the present decision on the question of the effect of the local law. In the present case the effect to be given to the local law is not material, since the decision would go against the petitioner whatever effect may be given to the local law. Consequently, this conflict does not warrant certiorari in the present case.

III

The Coal Company contends that the annual depletion allowable, in those years in which the tonnage mined was less than the tonnage which its lessees had the right to mine for the minimum royalty payment, should be based upon the minimum payment and not upon the number of tons actually extracted. This issue was raised by petitioner for the first time upon a motion for a rehearing at the hearing upon the recomputation of the deficiencies under Rule 50 of the Board's rules of practice, and the petitioner offered to prove the facts to sustain its contention that it would increase the amount of deduction allowable. (R. 68.) The Board denied the motion. (R. 69–70.) The Circuit Court of Appeals held it was within the sound discretion of the Board to grant or deny petitioner's motion, and the court could not say that there was an abuse of discretion. (R. 129.)

It is provided in Article 215 (b) of Regulations 45 (*infra*, p. 20) that in a case in which the required annual payment is regarded as the royalty for the equivalent number of units whenever the same shall be thereafter extracted and removed from the premises, the allowable deduction in the year of payment may be based on the number of units so paid for; and no deduction is permitted in subsequent years on account of the extraction of mineral so paid for.

But it appears that even if the case were reopened, petitioner would not be entitled to the deduction claimed. The theory upon which the claim is based is that the amount by which the minimum royalty received exceeds the total per ton royalty upon the coal actually extracted within the year, is an advance payment of royalty on coal which may be mined by the lessees in the future without further ro alty payments. The specimen lease introduced in evidence and which, it was testified, is typical of the others, provides for a fixed annual payment "as a minimum rental or royalty for the property," whether the quantity of coal mined and coke manufactured should produce that amount of royalty or not. The right of the lessees to mine coal thereafter free from royalty payment extended only to the next succeeding year and then it applied only to quantities above such amount as would be paid for by the minimum royalty in that year. Except on these two conditions, there was no right in the lessees to mine coal for past payments, and the findings indicate that there was very little, if any, coal mined upon the conditions mentioned. This is shown by the records of the mines operated by the lessees. (R. 44–46.) At the Fall River Pocahontas Collieries, the tonnage mined each year was the same as that paid for; at the Superior (Cletus) and at the Exeter Mines, the amount mined each year was always less than that paid for; at the Pocahontas Smokeless Coal Company mine the tonnage mined was substantially the

same as that paid for except as to the year 1920, when the amount mined was greater than that paid for, and this would affect only the year 1919, which is not involved here; at the Warwick and Hensley mines there are some variations, but they are not such as can be accounted for by the application of the minimum royalty provision mentioned above. (R. 44–46.)

Petitioner urges that the decision of the court below on this issue is in conflict with the decision in *Murphy Oil Co.* v. *Burnet,* 55 F. (2d) 17 (C. C. A. 9th), now pending in this Court (No. 80) on a writ of certiorari granted May 31, 1932. We believe the case at bar is distinguishable from the *Murphy Oil* case. There a substantial cash payment was made to the lessor upon the execution of an oil lease, in addition to which regular royalties were to be paid. The question was whether such payment was to be treated as entirely capital, entirely income or partly capital and partly income for purposes of adjusting the basis for depletion. In the case at bar, the payments were minimum annual rentals or royalties and did not result in a continuing right in the lessees to mine coal therefor. The lessees' right to mine coal for past payments was limited and conditional; the conditions under which coal could be mined free from royalties apparently did not arise in any of the years in question, and therefore the petitioner's property was not depleted either in fact or in theory because of the excess of minimum payments over the equivalent royalty of the tonnage extracted.

IV

The Coal Company contends that the decision of the District Court in the action brought by it against the Collector of Internal Revenue to recover taxes paid for earlier years is *res adjudicata* on the question of the rate of depletion to be allowed. We submit that the doctrine is not applicable because the parties are different and, in addition, because different causes of action or rights were involved since the two actions involve different taxable years.

The present proceeding is in effect a proceeding against the United States. While the Commissioner of Internal Revenue is the nominal party, he is proceeded against in his official and representative capacity as an officer of the United States, which is the real party in interest. The proceeding was brought by the taxpayer to review a determination of the Commissioner that the taxpayer is indebted to the United States for additional taxes. On the other hand, the suit in the district court was against the Collector of Internal Revenue. In *Sage* v. *United States,* 250 U. S. 33, this Court held that the United States was not privy to a judgment against a collector of internal revenue, and that the judgment is not a bar in a suit brought against the United States in the Court of Claims involving a part of the same tax. In that case, this Court pointed out that the suit against the collector is personal and its incidents are different. We believe that the petitioner's argument that the Commissioner is

privy to the suit against the collector is fully answered by what this Court said in the *Sage* case, which the court below accepted as controlling upon this question. See also *Graham & Foster* v. *Goodcell,* 282 U. S. 409, 430; *Smietanka* v. *Indiana Steel Co.,* 257 U. S. 1, 4, 5. Cf. *Union Trust Co.* v. *Wardell,* 258 U. S. 537; *United States* v. *Stone & Downer,* 274 U. S. 225.

CONCLUSION

The decision of the court below is correct and no sufficient reason appears for review by this Court. The petition should be denied.

Respectfully submitted.

THOMAS D. THACHER,
Solicitor General.
G. A. YOUNGQUIST,
Assistant Attorney General.
WHITNEY NORTH SEYMOUR,
SEWALL KEY,
ANDREW D. SHARPE,
Special Assistants to the Attorney General.
ERWIN N. GRISWOLD,
Attorney.

JULY, 1932.

APPENDIX

Statutes and Regulations Involved

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077:

> Sec. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> * * * * *
>
> (9) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost including cost of development not otherwise deducted: *Provided,* That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: * * * such reasonable allowance in all the above cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee.

Revenue Act of 1921, c. 136, 42 Stat. 227, 254:

> Sec. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> * * * * *

(9) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost including cost of development not otherwise deducted: *Provided,* That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: * * * such reasonable allowance in all the above cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee.

Revenue Act of 1924, c. 234, 43 Stat. 253, 283:

SEC. 234. (a) In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

* * * * *

(8) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee. (U. S. C., Title 26, Sec. 986.)

Revenue Act of 1926, c. 27, 44 Stat. 9, 41:

SEC. 234. (a) In computing the net income of a corporation subject to the tax im-

posed by section 230 there shall be allowed as deductions:

* * * * *

(8) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee. (U. S. C. App., Title 26, Sec. 986.)

Treasury Regulations 45 (1920 Edition):

ART. 215. *Depletion—Adjustments of accounts based on bonus or advanced royalty.*—(a) Where a lessor receives a bonus or other sum in addition to royalties, such bonus or other sum shall be regarded as a return of capital to the lessor, but only to the extent of the capital remaining to be recovered through depletion by the lessor at the date of lease. If the bonus exceeds the capital remaining to be recovered, the excess and all the royalties thereafter received will be income and not depletable. If the bonus is less than the capital remaining to be recovered by the lessor through depletion, the difference may be recovered through depletion deductions based on the royalties thereafter received. The bonus or other sum paid by the lessee for a lease made on or after March 1, 1913, will be his value for depletion as of date of acquisition.

(b) Where the owner has leased a mineral property for a term of years with a requirement in the lease that the lessee shall extract and pay for, annually, a specified

number of tons, or other agreed units of measurement, of such mineral, or shall pay, annually, a specified sum of money which shall be applied in payment of the purchase price or royalty per unit of such mineral whenever the same shall thereafter be extracted and removed from the leased premises, the value in the ground to the lessor, for purposes of depletion, of the number of units so paid for in advance of extraction will constitute an allowable deduction from the gross income of the year in which such payment or payments shall be made; but no deduction for depletion by the lessor shall be claimed or allowed in any subsequent year on account of the extraction or removal in such year of any mineral so paid for in advance and for which deduction has once been made.

(c) If, for any reason, any such mineral lease shall be terminated or abandoned before the mineral which has been paid for in advance has been extracted and removed, and the lessor repossesses the leased property, the lessor shall adjust his capital accounts by restoring to the capital sum of the property the depletion deductions made in prior years on account of royalties on mineral paid for but not removed, and his income account shall be adjusted so as to include the amount so restored to capital sum as income of the year such lease is terminated or the property repossessed, and the tax thereon paid.

(d) Upon the expiration, termination, or abandonment of a lease, without the removal of any or all of the mineral contemplated by the lease, the lessor shall be required to restore to capital account so much of the bonus received and deducted from capital recover-

able through depletion as is in excess of the actual depletion or loss in value sustained as a result of the operations under the lease and the corresponding amount will be income for the year in which the lease expires, terminates, or is abandoned.

Paragraphs (b) and (c) of the above article appear in the same form in Article 215 of Regulations 62, and Articles 216 of Regulations 65 and 69, and in Article 236 of Regulations 74.

Paragraphs (a) and (d) originally appeared in the same form as above in Article 215 of Regulations 62 and Article 216 of Regulations 65, but were afterwards amended by T. D. 3938, C. B. V–2, pp. 117–118, promulgated November 13, 1926, to read as follows:

Article 215 of Regulations 45 (1920 edition), article 215 of Regulations 62, and article 216 of Regulations 65 are hereby amended to read as follows:

ART. 216 (215). *Depletion—Adjustments of accounts based on bonus or advanced royalty.*—(a) Where a lessor receives a bonus in addition to royalties, there shall be allowed as a depletion deduction in respect of the bonus an amount equal to that proportion of the cost or value of the property on the basic date which the amount of the bonus bears to the sum of the bonus and the royalties expected to be received. Such allowance shall be deducted from the amount remaining to be recovered by the lessor through depletion, and the remainder is recoverable through depletion deductions on the basis of royalties thereafter received.

* * * * *

(d) Upon the expiration, termination, or abandonment of the lease, without the removal of any or all of the mineral contemplated by the lease, the lessor shall be required to restore to capital account the excess of the depletion theretofore allowable in respect of the bonus and royalty payments over the actual depletion or loss in value sustained as a result of the operations under the lease, and a corresponding amount must be returned as income for the year in which the lease expires, terminates, or is abandoned.

All rulings inconsistent herewith are hereby revoked.

Paragraphs (a) and (d) as thus revised appear in Article 216 of Regulations 69 and, with immaterial changes, in Article 236 of Regulations 74.

U. S. GOVERNMENT PRINTING OFFICE: 1932

FILE COPY

FILED
NOV 15 193
CHARLES ELMORE C

Nos. 104 and 105

In the Supreme Court of the United States

OCTOBER TERM, 1932

BANKERS POCAHONTAS COAL COMPANY, PETITIONER
v.
DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

D. J. F. STROTHER, PETITIONER
v.
DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT

INDEX

	Page
Opinions below	1
Jurisdiction	2
Questions presented	2
Statutes and regulations involved	3
Statement	3
Summary of argument	8
Argument:	
I. Royalties received by petitioner Bankers Pocahontas Coal Company under the lease agreements are taxable income	11
II. The judgment of the United States District Court for the Southern District of West Virginia in the case of *Bankers Pocahontas Coal Company* v. *White, Collector*, is not *res judicata* of the issue in the case at bar of the reasonable depletion rate	19
III. There is no error in the ruling of the lower court sustaining the Board of Tax Appeals in its refusal to receive additional evidence at the hearing upon settlement of the amount of the deficiency and subsequent to promulgation of its findings of fact and opinion	25
Conclusion	33
Appendix	34–43

CITATIONS

Cases:	
Alexander v. *King*, 46 F. (2d) 235, certiorari denied, 283 U. S. 845	14
Berg v. *Commissioner*, 33 F. (2d) 641, certiorari denied, 280 U. S. 598	14
Bertelsen v. *White*, 58 F. (2d) 792	25
Boggs & Buhl v. *Commissioner*, 34 F. (2d) 859	27
Burkett v. *Commissioner*, 31 F. (2d) 667, certiorari denied, 280 U. S. 565	15
Burnet v. *Harmel*, No. 26, October Term, 1932	14, 16
Burnet v. *Logan*, 283 U. S. 404	16
Burnet v. *Sanford & Brooks Co.*, 282 U. S. 359	22
Coal & Coke Co. v. *Tax Commissioner*, 59 W. Va. 605	17
Commissioner v. *Old Colony R. R.*, 26 F. (2d) 408, dismissed, 279 U. S. 876	22
Commissioner v. *Old Colony R. Co.*, 50 F. (2d) 896	22
Feather v. *Baird*, 85 W. Va. 267	18

Cases—Continued.	Page
Ferguson v. *Commissioner*, 45 F. (2d) 573	14
Goldsmith v. *Board of Tax Appeals*, 270 U. S. 117	26
Graham & Foster v. *Goodcell*, 282 U. S. 409	21
Great Northern Ry. Co., 10 B. T. A. 1347, aff'd, 40 F. (2d) 372, certiorari denied, 282 U. S. 855	27
Greengard v. *Commissioner*, 29 F. (2d) 502	26
Greylock Mills v. *White*, 55 F. (2d) 704	25
Handy & Harman v. *Burnet*, 284 U. S. 136	24
Hirschi v. *United States*, 67 C. Cls. 637, certiorari denied, 280 U. S. 576	14
Jefferson Gas Coal Co. v. *Commissioner*, 52 F. (2d) 120	15
Lynch, Executrix v. *Alworth-Stephens Co.*, 267 U. S. 364	13
Maney v. *United States*, 278 U. S. 17	23
Metropolitan Business College v. *Blair*, 24 F. (2d) 176	27
Murphy Oil Co. v. *Burnet*, No. 80, October Term, 1932	28
National Coal Co. v. *Overholt*, 81 W. Va. 427	18
New Orleans v. *Citizens' Bank*, 167 U. S. 371	24
O'Meara v. *Commissioner*, 34 F. (2d) 390	27
Old Colony Trust Co. v. *Commissioner*, 279 U. S. 716	21
Old Colony R. Co. v. *Commissioner*, 284 U. S. 552	13, 22
Reinecke v. *Spalding*, 280 U. S. 227	14
Rosenberger v. *McCaughn*, 25 F. (2d) 699, certiorari denied, 278 U. S. 604	14, 15
Sage v. *United States*, 250 U. S. 33	20, 21
Second Nat. Bank v. *Woodworth*, 54 F. (2d) 672	25
Smietanka v. *Indiana Steel Co.*, 257 U. S. 1	21
Smith v. *Root*, 66 W. Va. 633	19
Sooy v. Commissoner, 40 F. (2d) 634	27
Stanton v. *Baltic Mining Co.*, 240 U. S. 103	12, 13
Stratton's Independence, Limited v. *Howbert*, 231 U. S. 399	12, 13
Taylor v. *Thomas*, 106 W. Va. 376	18
Toothman v. *Courtney*, 62 W. Va. 167	19
Tutun v. *United States*, 270 U. S. 568	23
Union Trust Co. v. *Wardell*, 258 U. S. 537	21
United States v. *Biwabik Mining Co.*, 247 U. S. 116	13
United States v. *Ness*, 245 U. S. 319	22
United States v. *Stone & Downer Co.*, 274 U. S. 225	23, 24
Urpman v. *Lowther Oil Co.*, 53 W. Va. 501	19
Von Baumbach v. *Sargent Land Co.*, 242 U. S. 503	12, 13
Constitution and Statutes:	
Constitution of the United States—	
Article 1, Section 9, Clause 4	34
Sixteenth Amendment	34
Revenue Act of 1918, c. 18, 40 Stat. 1057, 1065, 1077—	
Sec. 213	34
Sec. 234	35

Constitution and Statutes—Continued. Page

Revenue Act of 1921, c. 136, 42 Stat. 227, 237, 254, 264, 314—
Sec. 213 35
Sec. 234 35
Sec. 250 21
Sec. 1318 (U. S. C., Title 26, Sec. 156) 22
Revenue Act of 1924, c. 234, 43 Stat. 253, 267, 283, 297, 343—
Sec. 213 (U. S. C., Title 26, Sec. 954) 36
Sec. 234 (U. S. C., Title 26, Sec. 986) 36
Sec. 274 (U. S. C., Title 26, Sec. 1048) 21
Sec. 1014 (U. S. C., Title 26, Sec. 156) 22
Revenue Act of 1926, c. 27, 44 Stat. 9, 23, 41, 55, 116—
Sec. 213 (U. S. C. App., Title 26, Sec. 924) 36
Sec. 234 (U. S. C. App., Title 26, Sec. 986) 36
Sec. 274 (U. S. C. App., Title 26, Sec. 1048) 37
Sec. 1113 (U. S. C. App., Title 26, Sec. 156) 38
Revenue Act of 1928, c. 852, Sec. 601, 45 Stat. 791, 871 (U. S. C. Sup, V, Title 26, Sec. 1219 (a)) 26

Miscellaneous:
Rule 50, Board of Tax Appeals 42–43
T. D. 3938, V–2 C. B., 117–118 40
Treasury Regulations 45, Art. 215 38
Treasury Regulations 62, Art. 215, Art. 216 40
Treasury Regulations 65, Art. 216 40
Treasury Regulations 69, Art. 216 ..... 40, 42
Treasury Regulations 74, Art. 236 ..... 40, 42

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 104

BANKERS POCAHONTAS COAL COMPANY, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

No. 105

D. J. F. STROTHER, PETITIONER

v.

DAVID BURNET, COMMISSIONER OF INTERNAL REVENUE

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FOURTH CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Board of Tax Appeals (R. 49–57)[1] is reported in 18 B. T. A. 901. The opinion of the Circuit Court of Appeals (R. 119–134) is reported in 55 F. (2d) 626.

---

[1] The record references are to the record in the *Bankers Pocahontas Coal Company case* (No. 104) unless otherwise indicated.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered in each case January 27, 1932. (R. 135–136; Strother R. 111.) A petition of the petitioners for a rehearing covering both cases was presented February 26, 1932. (R. 137–167; Strother R. 112–138.) A petition of the respondent for a rehearing in the *Strother case* was presented February 26, 1932. (Strother R. 139–141.) Both petitions were denied by an order entered March 7, 1932. (R. 169–170; Strother R. 141–142.) By leave of court, the petitioners filed a supplemental petition for rehearing on April 12, 1932. (R. 171–183; Strother R. 143–153.) The supplemental petition for rehearing was denied April 29, 1932. (R. 185; Strother R. 154.) The petition for certiorari was filed May 23, 1932, and was granted October 10, 1932. (R. 187.) Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether royalties received by the petitioner, Bankers Pocahontas Coal Company, under certain instruments made prior to March 1, 1913, are taxable income.

2. Whether a judgment against a Collector of Internal Revenue in an action brought by petitioner in a United States District Court, involving taxes for other taxable years than those in the present

case, is *res judicata* of the issue of the proper depletion rate.

3. Whether the Board of Tax Appeals should have granted a rehearing upon evidence presented by petitioners for the first time upon final settlement of the deficiency, and if so, whether the corporate petitioner was entitled to a further allowance for depletion?

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are contained in the Appendix, *infra,* pp. 34–43.

STATEMENT

The respondent determined deficiencies in income and profits taxes of the petitioner Bankers Pocahontas Coal Company for the years 1920 to 1926, inclusive, amounting to $39,851.99 (R. 12, 23, 29), and in income taxes of the petitioner Strother for the years 1919 to 1925, inclusive, amounting to $8,874.50 (Strother R. 11, 17, 23). The petitioners appealed from these determinations to the Board of Tax Appeals.

The material facts as found by the Board may be summarized as follows (R. 39–49):

The petitioner Bankers Pocahontas Coal Company (hereafter called the Coal Company) is a West Virginia corporation formed in 1912. In that year it acquired in fee 6,200 acres of land in West Virginia, including the mineral rights therein. Also, by assignment, it acquired and holds the interest of the prior owners in certain contracts

of lease executed in 1901 and 1902 with several coal operating companies, to which the tract of land was subject. By these contracts the prior owners did "demise, let and lease for coal mining and coal coking purposes only" for the period of thirty years to the coal operating companies, severally, certain parts of the tract. The form of contract used was that prevailing in the West Virginia coal fields, and followed the form used in the State of Pennsylvania. (R. 39–40.) Extracts from a typical contract appear at R. pp. 40–42. The cost to the Coal Company of the properties was between $407,000 and $507,000. (R. 42.)

Schedules appearing in the findings of fact (R. 43–46) contain a list of the contracts and show the estimated recoverable coal on March 1, 1913, and the number of tons mined, the number of tons paid for, and the royalty receipts in the taxable years here in question, under each contract.

In these years the Coal Company was on a cash receipts and disbursements basis of accounting. Its income, except for minor items, consisted of payments received under these contracts. (R. 46.)

The respondent treated the income derived from the contracts as royalty payments under leases, and allowed the Coal Company, as lessor, a deduction for depletion at the rate of 3.6 cents per ton of coal mined. This is the rate that had been allowed by the respondent for 1919 and prior years. (R. 47–48.)

Additional taxes amounting to $6,267.08 were assessed and collected for the years 1914 to 1919, in-

clusive. In 1923 the Coal Company brought an action in the District Court for the Southern District of West Virginia against the collector of internal revenue to recover those taxes. The Coal Company contended that payments received by it under the contracts were proceeds of the sale of coal in place consummated before March 1, 1913, or of choses in action owned on that date and therefore not income; or, otherwise, that in computing net income it was entitled as lessor to a depletion rate of 5 cents per ton of coal mined. The court held that the receipts were income and found that the plaintiff was entitled to a depletion rate of 5 cents a ton, and entered judgment in its favor for $5,373.01, which was paid. The Collector of Internal Revenue, as defendant, was represented in that action by the United States Attorney and the Solicitor of Internal Revenue (now General Counsel of the Bureau of Internal Revenue). (R. 47.)

In the several years here involved the petitioner Strother, as a stockholder, received payments from the Coal Company. He reported them in his income tax returns but did not include them as taxable income. The Coal Company used such portion of the royalty payments as was necessary for ordinary and necessary expenses, set aside a reserve to meet pending Federal taxes, and distributed the balance to its stockholders. The respondent added the entire amount thus distributed to Strother to his net income without allowance for any part thereof that might have come out of the depletion

reserve of the Coal Company. Deficiencies against Strother were determined by the respondent accordingly. (R. 72–73.)

In the case of the Coal Company, the Board of Tax Appeals held that the payments received by the petitioner under the contracts were royalties which were properly part of its gross income; that it was entitled to a reasonable allowance for depletion, and that the petitioner had failed to prove that the allowance determined by the respondent of 3.6 cents per ton was not reasonable. (R. 51, 54.) On February 27, 1930, the Coal Company filed with the Board a motion for a rehearing and alleged as error, among others, that the Board had failed to hold that the decision in the case of this petitioner against the Collector of Internal Revenue, in the United States District Court for the Southern District of West Virginia, was *res judicata* of the issue with respect to the depletion rate. (R. 57–59.) The motion was denied. (R. 59–60.) Upon final settlement of the amount of deficiencies under the Board's decision, petitioner filed objections to the proposed determinations submitted by respondent and presented counter proposed determinations. The Coal Company therein contended for the first time that the depletion allowance should be on the basis of the minimum royalty payments and not upon the tonnage of coal mined, where the latter was less than was permitted to be mined for the minimum royalty payment in any year. (R. 66–

69.) At the oral hearing on final settlement, a motion was made on behalf of both petitioners for a rehearing to enable them to offer additional evidence for the purpose of raising this question, and the Board denied the motion. (R. 69–70, 109–110.) The Board thereupon entered its order in the *Coal Company case* redetermining the deficiencies in the aggregate amount of $39,171.05. (R. 70–71.) The Circuit Court of Appeals sustained the decision of the Board on all of the above issues.[2]

In the *Strother case,* before the Board, it was agreed between the parties that the distributions received by Strother were nontaxable to the extent that they came out of the depletion reserve of the Coal Company. (R. 57.) The respondent thereupon filed a proposed settlement of the amount of the deficiencies. (Strother R. 49–56.) The petitioner Strother filed objections and a counter proposal alleging error, among others, in the respondent's computation in that it did not accord with the allowances for depletion made to the Coal Company. (Strother R. 57–63, 64–70.) After oral hearing (Strother R. 81–87) the Board adopted the computations of the respondent and entered its order redetermining deficiencies aggregating $5,806.07 and an overassessment for the year 1924 to be abated in the amount of $36.38. (Strother R. 71–72.) The Circuit Court of Appeals decided

[2] There were certain other issues before the Board and the Circuit Court in the *Coal Company case* which are not involved in the present petition.

Strother should be given an opportunity to introduce additional testimony on the issues raised by him on the hearing on final settlement, and it remanded this case for further proceedings in accordance with its opinion in the *Coal Company case*. (Strother R. 110.) As it was stipulated that decision in the *Strother case* should follow that in the *Coal Company case* as to the issues now presented (Strother R. 80) no further separate discussion of that case seems to be necessary.

SUMMARY OF ARGUMENT

1. Royalties received from a lessee of coal lands in West Virginia, upon leases made prior to the enactment of the Sixteenth Amendment, constitute gross income. To impose a tax upon such receipts does not violate the Constitution of the United States as being an unapportioned direct tax.

It is clear from the comprehensive definition of gross income contained in the Revenue Acts, and the decisions of this Court and of Circuit Courts of Appeals with respect thereto, that Congress intended to tax such income.

It is immaterial that, as assumed by the court below for the purposes of the present case, such leases are construed by the courts of West Virginia as effecting a sale of the mineral in place. The royalties received from such leases are nevertheless taxable under the Federal statute, subject only to an allowance for depletion. Furthermore,

an examination of the decisions of the highest court of West Virginia shows that the decisions are not uniform, and that there is doubt whether this is the established law of that State. Whatever may be the legal effect of these instruments under the State law, the royalties received thereunder are properly gross income under the provisions of the Revenue Act and the decisions of this Court.

2. The judgment of the District Court in the action by the Coal Company against the Collector of Internal Revenue, in an action involving taxes for different taxable years from those involved here, is not *res judicata* of the issue of the correct depletion rate. That rule has no application to a case like this where the parties are different, different causes of action or rights are involved, and the statute expressly authorizes maintenance of a new suit for each taxable year.

3. There is no error in the ruling of the court below sustaining the Board of Tax Appeals in its refusal to receive evidence first offered at the hearing on recomputation of the tax under Rule 50 of the Board on an issue not raised in the pleadings or presented at the hearing on the merits. Denial of such rehearing was proper under the rule of the Board relating to hearings for final settlement. That rule is valid and the denial was also a proper exercise of discretion.

Petitioner's contentions thus advanced too late were that the depletion allowance should be based

upon the minimum annual royalties instead of upon the number of tons of coal actually extracted, where the minimum annual payments exceed the royalties, at the per ton rate on coal extracted. But the right of the lessees to mine coal to offset the excess of royalty paid in any year was limited to the next succeeding year after the amount necessary to produce the minimum royalty for that year had been mined. The present case, therefore, is not within the terms of the Treasury regulations providing that advance royalties are subject to depletion allowance. But from facts found by the Board of Tax Appeals it appears that royalty payments on coal extracted exceeded the required minimum annual payments—with a possible exception in the case of one lease, depending upon a particular construction of the facts. Even if that construction of the facts should be adopted, it will appear that in only three years was there a deficiency in coal mined, and as to only one of those years was the deficiency offset in part in the next year. Hence, if it should be held that the principle of the regulations should be applied in the present case, there would be no substantial change in the result, for the Coal Company will be required to restore to capital account and to report as income in the succeeding year any excess of depletion allowed in the preceding year.

ARGUMENT

I

ROYALTIES RECEIVED BY PETITIONER BANKERS POCAHONTAS COAL COMPANY UNDER THE LEASE AGREEMENTS ARE TAXABLE INCOME

The Circuit Court of Appeals held that, even though the instruments here in question are construed under the law of West Virginia as effecting a sale of coal in place, the per ton royalty payments or the annual minimum rental payments provided for therein constitute gross income to the Coal Company. Petitioners' contention seems to be, first, that the decision violates Article 1, Sec. 9, Clause 4, of the Constitution in that it authorizes a direct tax upon property without apportionment, i. e., upon the proceeds of a sale of property made prior to the effective date of the Amendment,[3] and next, that Congress did not intend to tax such receipts.

We submit that both of these contentions have been fully answered by previous decisions of this Court. In *Stanton* v. *Baltic Mining Co.*, 240 U. S.

[3] It appears from the statement of petitioners' counsel in connection with petitioners' motion for a rehearing (discussed under Point III of this brief), that in the case of two of the leases new instruments were executed after March 1, 1913, to wit, September 30, 1916, and January 1, 1918, "each reciting the pre-existence of contracts on March 1, 1913, and the subsequent adjustment and modification of same as to payments of a minimum royalty * * *." (R. 109, 110.)

103, which arose under the income-tax provisions of the Tariff Act of 1913, c. 16, Sec. 2, 38 Stat. 166, 181, it was contended that the proceeds of mining without an adequate allowance by way of deduction for exhaustion of the ore body was a tax upon property because of its ownership and therefore subject to the constitutional requirement of apportionment. Of this contention, this Court said (pp. 113–114):

> It moreover rests upon the wholly fallacious assumption that looked at from the point of view of substance a tax on the product of a mine is necessarily in its essence and nature in every case a direct tax on property because of its ownership unless adequate allowance be made for the exhaustion of the ore body to result from working the mine. We say wholly fallacious assumption because independently of the effect of the operation of the Sixteenth Amendment it was settled in *Stratton's Independence* v. *Howbert,* 231 U. S. 399, that such a tax is not a tax upon property as such because of its ownership, but a true excise levied on the results of the business of carrying on mining operations (pp. 413 *et seq.*). (Citing *Brushaber* v. *Union Pacific R. R.,* 240 U. S. 1.)

That case and *Stratton's Independence, Limited,* v. *Howbert,* 231 U. S. 399, involved the proceeds of ore mined by a corporation from its own premises. *Von Baumbach* v. *Sargent Land Co.,* 242 U. S. 503, involved moneys received from lessees under in-

struments which were in form mining leases for terms of fifty years. The question was whether the receipts were income under the corporation excise tax provisions of the Tariff Act of 1909, c. 6, 36 Stat. 11, 12. This Court decided, on the principles announced in the *Baltic Mining Co.* and *Stratton's Independence cases, supra*, that the royalties received under the leases were income, and it referred to its holding in the *Stratton's Independence case* that the process of mining is in a sense equivalent to a manufacturing process, and that however the operation is described it is indubitably business and the gains derived from it are properly income derived from capital, from labor, or from both combined. This Court also held that it made no difference whether the ores were extracted by the mine owner, as in the *Stratton's Independence case,* or by a lessee of the owner, as in the case of the *Sargent Land Company.* (p. 521.) See also *United States* v. *Biwabik Mining Co.,* 247 U. S. 116; *Lynch, Executrix,* v. *Alworth-Stephens Co.,* 267 U. S. 364.

The case of *Old Colony R. Co.* v. *Commissioner,* 284 U. S. 552, is not in point, as the question there was whether a *pro rata* part of premiums received upon the sale of the petitioner's bonds prior to 1913 should be included in gross income of 1921 or should reduce the item of interest paid which is permitted as a deduction from gross income. The holding of

this Court was that such premium is income for the year in which it was received, and no part thereof could be income for any other year. In the case at bar, while the instruments in question were entered into prior to the adoption of the Sixteenth Amendment, at that time the Coal Company was the owner of the right to receive royalties as stipulated in the instruments and to regain possession when the leases terminated. The situation of the Coal Company is precisely like that of the respondent in *Reinecke* v. *Spalding,* 280 U. S. 227. In that case the respondent received royalties under leases made prior to 1913, and the effect of this Court's decision is that the royalties received are income against which the taxpayer is entitled to deduct as depletion the per unit value on March 1, 1913, of the right to receive the royalties.

In view of the comprehensive definition of gross income contained in Section 213 (a) of the relevant Revenue Acts (*infra,* p. 34), and the decisions of this Court, there would seem to be no doubt that Congress intended to tax such income. See *Burnet* v. *Harmel,* No. 26, October Term, 1932, decided November 7, 1932; *Hirschi* v. *United States,* 67 C. Cls. 637, certiorari denied, 280 U. S. 576; *Rosenberger* v. *McCaughn,* 25 F. (2d) 699 (C. C. A. 3d), certiorari denied, 278 U. S. 604; *Alexander* v. *King,* 46 F. (2d) 235 (C. C. A. 10th), certiorari denied, 283 U. S. 845; *Ferguson* v. *Commissioner,* 45 F. (2d) 573 (C. C. A. 5th); *Berg* v. *Commissioner,* 33

F. (2d) 641 (App. D. C.), certiorari denied, 280 U. S. 598; *Burkett* v. *Commissioner,* 31 F. (2d) 667 (C. C. A. 8th), certiorari denied, 280 U. S. 565.

The *Rosenberger case, supra,* involved the question whether royalty payments under a lease of Pennsylvania coal lands similar to the leases involved in the instant case were taxable income. The Circuit Court of Appeals held that they were, although it recognized that under Pennsylvania law such leases constitute a sale of coal in place. The later decision of the Circuit Court of Appeals for the Third Circuit in *Jefferson Gas Coal Co.* v. *Commissioner,* 52 F. (2d) 120, is not to the contrary. The question there was the right of the petitioner to deduct from income, payments made under an agreement called a " lease " entered into in 1920 and providing for the payment of a certain rate per ton for coal mined or minimum annual payments over a period of ten years. The coal mined in the first three years was considerably less than would, at the per ton rate, equal the minimum payments. The court held that the petitioner could deduct only the amount of the royalty rate on the coal mined and not the total amount of the minimum payments, because the agreement provided that whenever the total payments made equalled the aggregate of the minimum annual royalty payments for ten years the petitioner was entitled to a deed in fee simple, free of encumbrances, for all of the

unmined coal in the lands in question. The instrument was held to be a contract of sale, and the minimum payments were held to be payments on the purchase price and hence capital expenditures. The cases are plainly distinguishable.

The present case is also distinguishable from *Burnet* v. *Logan,* 283 U. S. 404, as that case involved the calculation of gain on the sale of stock, and this Court expressly observed that it was not dealing with royalties or deductions from gross income because of depletion of mining property. (P. 412.)

The Circuit Court of Appeals assumed for the purposes of its decision herein, that under the law of West Virginia a mining lease constituted a sale of the mineral in place, and it held that nevertheless the royalties in question were taxable income (R. pp. 123–124), since the power of Congress to tax their receipt was not limited by the construction placed upon such instruments by the state courts. The view taken by the court below is sustained by the decision of this Court in *Burnet* v. *Harmel, supra,* decided November 7, 1932. In that case this Court held that a bonus received in connection with a lease of oil lands in Texas was taxable as ordinary income and not as a gain from the sale of capital assets. This Court said:

> Bonus and royalties are both consideration for the lease and are income of the lessor.

The Court held that the fact that leases of oil lands were regarded by the Texas courts as sales of oil in place did not affect the nature of bonuses as ordinary income under the Federal Revenue Acts. We believe that this decision practically disposes of this branch of the case.

Although the court below assumed that the instruments involved would be held under the state law to convey title to the mineral in place, an examination of the decisions of the Supreme Court of Appeals of West Virginia indicates that this is not the established law, or at least that the state decisions are not uniform on the point.

In *Coal & Coke Co.* v. *Tax Commissioner,* 59 W. Va. 605, the court, in applying a West Virginia statute which provided for the taxation of personal property, held that a mining lease, similar in all substantial respects to the instruments involved in the present case, was a chattel real taxable to the lessee as personalty. The lessee had contended that the deed amounted to a sale of the coal in place, taxable only as realty. The court said (p. 611):

> Try this property or right under these definitions. It is surely a lease, and therefore a chattel real. The fee owner carves out of his fee a particular estate and vests it in another. The coal having been developed, then, if not before, an actual estate vested as to the coal right, an entity, a distinct entity, a separate property from that

> remaining in the lessor. The instrument of conveyance gave certain title to the Coal Company, gave it an intangible right, that is, a right to produce personal property, a product of the land. This right savored of the realty, depended on it, was annexed to it, and so far answers the definition of a chattel real, which is personal estate. We say that the estate of the coal company is a lease for years, and if so, by all authority, is a chattel real. The parties thought they were making a lease for years, intended to do so, so far as we may judge from legal language, for they used the words of lease signification, "demise, lease, and let." The instrument calls itself a lease and calls the parties lessor and lessee. But take the document itself. It leases the tract for "a period of thirty years," not forever. It has a specific term, gives an estate less than the fee of the lessors, leaving the whole tract at the end of the term to revert to the lessors disencumbered and freed from the leasehold estate, thus meeting another element in the definition of a chattel real, that is, that it must be of less duration than the estate of the lessor. * * *

Expressions in *National Coal Co.* v. *Overholt,* 81 W. Va. 427, to the effect that the instrument there involved constituted a sale of coal in place do not seem to have been strictly necessary to decision, but in any event were based upon a construction of the particular instrument. Cf. *Taylor* v. *Thomas,* 106 W. Va. 376, and *Feather* v. *Baird,* 85 W. Va. 267.

Urpman v. *Lowther Oil Co.*, 53 W. Va. 501; *Toothman* v. *Courtney*, 62 W. Va. 167; *Smith* v. *Root*, 66 W. Va. 633.

We believe it can not be said that it is the established law of West Virginia that instruments such as these involved in the case at bar convey title to the mineral in place. But we submit that in any view of the legal effect of these instruments under state law, the royalties received by the Coal Company were properly included in gross income.

II

THE JUDGMENT OF THE UNITED STATES DISTRICT COURT FOR THE SOUTHERN DISTRICT OF WEST VIRGINIA IN THE CASE OF BANKERS POCAHONTAS COAL COMPANY V. WHITE, COLLECTOR, IS NOT RES JUDICATA OF THE ISSUE IN THE CASE AT BAR OF THE REASONABLE DEPLETION RATE

The case of *Bankers Pocahontas Coal Co.* v. *White, Collector,* involved the depletion allowance of petitioner for the years from 1914 to 1919, inclusive. (R. 89.) The District Court allowed a depletion rate of 5 cents a ton. (R. 95.) The present proceeding relates to the years 1920 to 1926, inclusive. (R. 38.) The respondent determined that 3.6 cents per ton was a proper depletion rate for these years, and the Board of Tax Appeals held that the Coal Company had failed to prove that this rate was erroneous. (R. 53–54.) The court below sustained the Board. (R. 127–128.) The Coal Company contends that the rate of deple-

tion allowed by the District Court for prior years in an action brought by it against the Collector of Internal Revenue is *res judicata* of the issue of depletion in the instant case. We submit that the doctrine is not applicable because the parties are different, different causes of action or rights are involved, and separate suits or proceedings are specifically authorized by statute. We assume for the purpose of the argument that the fact that the judgment is pleaded in the Board of Tax Appeals and not in a court is not material.

The present proceeding is in effect a proceeding against the United States. While the Commissioner of Internal Revenue is the nominal party, he is proceeded against in his official and representative capacity as an officer of the United States, which is the real party in interest; it is the United States which will be concluded by any decision adverse to the Commissioner. The proceeding is brought with its consent to review a determination of the Commissioner that the taxpayer is indebted to the United States for additional taxes. On the other hand, the suit in the District Court was against the Collector of Internal Revenue. In *Sage* v. *United States,* 250 U. S. 33, this Court held that the United States was not privy to a judgment against a collector of internal revenue, and that the judgment was not a bar in a suit brought against the United States in the Court of Claims involving a part of the same tax. In that case, this Court pointed out that the suit against the collector is

personal and its incidents are different. We believe that the petitioners' argument that the Commissioner is privy to the suit against the collector is fully answered by what this Court said in the *Sage case, supra,* which the court below accepted as controlling upon this question. That case was cited with approval by this Court in *Graham & Foster* v. *Goodcell,* 282 U. S. 409, 430. See also *Smietanka* v. *Indiana Steel Co.,* 257 U. S. 1, 4, 5. Cf. *Union Trust Co.* v. *Wardell,* 258 U. S. 537.

The present action relates to taxes for different years from those involved in the suit in the District Court. A taxpayer is authorized to bring a proceeding for review to the Board of Tax Appeals in any case of a deficiency in tax found by the Commissioner. The Board was created to provide taxpayers an opportunity to secure an "independent review" of the Commissioner's determination. It is authorized to consider deficiencies beyond those stated by the Commissioner in his notice to the taxpayer and may also determine that the taxpayer has made an overpayment. Upon the Board's decision, "the parties are given an opportunity to base a petition for review to the courts." *Old Colony Trust Co.* v. *Commissioner,* 279 U. S. 716, 721, 722, 725. Section 274 (a), Revenue Act of 1926, c. 27, 44 Stat. 9 (U. S. C. App., Title 26, Sec. 1048.)[4] By Section 3226 of the Revised Statutes

[4] See also Section 250, Revenue Act of 1921, c. 136, 42 Stat. 227; Section 274, Revenue Act of 1924, c. 234, 43 Stat. 253 (U. S. C., Title 26, Sec. 1048).

(as amended by Section 1113 (a) of the Revenue Act of 1926 (U. S. C. App., Title 26, Sec. 156),[5] a taxpayer is authorized to maintain a suit for the recovery of *any* internal revenue tax alleged to have been erroneously assessed or collected, after certain prerequisites, such as claim for refund to the Commissioner, have been complied with. In view of these provisions, it may not be said that a judgment as to one taxable year is intended to be a bar to an action involving a tax for a different year.

Each year is treated as a unit (*Burnet* v. *Sanford & Brooks Co.*, 282 U. S. 359), and the procedure to collect, as well as the procedure to recover, must be followed with respect to each year in controversy. The statutes authorize suits with respect to one year's tax irrespective of the status of another year's tax. It has never been supposed that a decision upon a tax question was forever binding between the parties.[6]

This Court has held that where cumulative remedies are given by statute the doctrine of *res judicata* is not a bar to a second suit. *United States*

[5] See also Section 1318, Revenue Act of 1921, c. 136, 42 Stat. 227 (U. S. C., Title 26, Sec. 156); Section 1014 (a), Revenue Act of 1924, c. 234, 43 Stat. 253 (U. S. C., Title 26, Sec. 156).

[6] For example, in *Old Colony R. Co.* v. *Commissioner*, 284 U. S. 552, it appears that the question had been previously litigated between the same parties. *Commissioner* v. *Old Colony R. R.*, 26 F. (2d) 408 (C. C. A. 1st), writ of certiorari dismissed, 279 U. S. 876; *Commissioner* v. *Old Colony R. Co.*, 50 F. (2d) 896 (C. C. A. 1st).

v. *Ness,* 245 U. S. 319. See also *Maney* v. *United States,* 278 U. S. 17, 23; *Tutun* v. *United States,* 270 U. S. 568, 580.

In *United States* v. *Stone & Downer Co.*, 274 U. S. 225, 230, it was taken as settled that the doctrine of *res judicata* may apply to cases of taxes as well as to other subjects of litigation, but the doctrine was not applied in that case for reasons which are equally pertinent here. That case dealt with the proper classification of an importation of wool for the purpose of applying the correct tariff rate. Although there had been a prior judgment by the Court of Customs Appeals applying one classification to the wool, that court had established the practice that a decision upon a finding of fact, a construction of the statute and classification thereunder, was not *res judicata* in respect of a subsequent importation.

The purpose of that practice was to avoid inequality and discrimination in the administration of the customs laws which would result from giving a permanently binding effect to a decision favorable to a particular importer. Much of this reasoning (pp. 235–237) is applicable to tax cases arising under the revenue laws, for it is apparent that the application of the doctrine would result in inequality in the administration of the revenue laws and give preference to those taxpayers who successfully litigated a tax question, over others who may be subject to tax liability as the result of a later deci-

sion of controlling authority laying down a different rule. For example, if the interpretation of the affiliation statutes by this Court in *Handy & Harman* v. *Burnet,* 284 U. S. 136, may not be applied to all corporations without regard to erroneous decisions granting affiliation in prior years, discrimination, injustice, and confusion will result. The startling results of such a rule can hardly be exaggerated. If any such rule should prevail the interests of the Government could not be adequately protected unless appeals were taken and writs issued by this Court to review every questionable decision in a Government tax case. For unless all such cases were brought to this Court there would be created a numerous class of taxpayers privileged in the permanent enjoyment of tax exemptions predicated upon the decisions of the lower Federal courts, later declared to be erroneous and overruled. Decisions of the courts in suits against a collector of taxes conclusively settle the validity of the tax collections in question. They should be given no wider scope. We submit that the principle laid down in *New Orleans* v. *Citizens' Bank,* 167 U. S. 371, should not be applied to tax cases involving different years for reasons similar to those which induced the Court not to apply it in the *Stone & Downer case* (p. 237).

The doctrine of *res judicata* has been applied in three recent cases in District Courts, but we believe that in each of those cases different situations were presented from that in the case at bar.

In *Second Nat. Bank* v. *Woodworth,* 54 F. (2d) 672 (E. D. Mich.), it was held that a judgment in favor of the United States in a suit based on rejection of a claim for refund of additional estate tax paid under protest was a bar to a subsequent suit against the Collector of Internal Revenue presenting the same issues. In that case attempt was made to relitigate questions as to the same tax. Similar situations were presented in *Greylock Mills* v. *White,* 55 F. (2d) 704 (Mass.), and in *Bertelsen* v. *White,* 58 F. (2d) 792 (Mass.).

We submit that for the reasons stated judgment of the District Court in the prior action was not a determination on the question of depletion which was binding in the present proceedings.

III

THERE WAS NO ERROR IN THE RULING OF THE LOWER COURT SUSTAINING THE BOARD OF TAX APPEALS IN ITS REFUSAL TO RECEIVE ADDITIONAL EVIDENCE AT THE HEARING UPON SETTLEMENT OF THE AMOUNT OF THE DEFICIENCY AND SUBSEQUENT TO PROMULGATION OF ITS FINDINGS OF FACT AND OPINION

After the Board of Tax Appeals had filed its findings of fact and opinion, the respondent and the petitioners each filed proposed recomputations of the amount of the deficiency under the Board's report. (R. 61–66, 66–69; Strother, 57–63.) These proposed recomputations were filed pursuant to Rule 50 of the Board's rules of practice (*infra,* p. 42). The petitioners, in their recomputations,

claimed that a greater quantity of coal was paid for than was mined, and that the depletion allowance should be computed on the basis of the amount of the payments received instead of upon the number of tons extracted. (R. 68; Strother 58.) At the hearing upon the recomputation under Rule 50, petitioners tendered evidence designed to support these claims. (R. 109–110; Strother 82, 86.) The question had not been raised previously in the pleadings nor at the hearing on the merits. That hearing was had in May, 1929. (R. 84.) The Board's findings and opinion were promulgated January 22, 1930. (R. 37.) Motion for a rehearing on this question was not made until May, 1930. (R. 66–69.) The Board denied the motion. (R. 69–70.) The Circuit Court of Appeals held that it was within the sound discretion of the Board to grant or to deny petitioners' motion; and that since the evidence must have been in the possession of the Coal Company from the beginning the court could not say that there had been an abuse of discretion. (R. 129.)

The Board is authorized to prescribe rules of practice and procedure for the conduct of proceedings before the Board. Section 601, Revenue Act of 1928, c. 852, 45 Stat. 791, 871–872 (U. S. C. Sup. V., Title 26, Sec. 1219 (a)), amending Section 907 (a) of the Revenue Act of 1924, as amended. See *Greengard* v. *Commissioner,* 29 F. (2d) 502, 503. (C. C. A. 7th). Cf. *Goldsmith* v. *Board of Tax Appeals,* 270 U. S. 117.

Rule 50 of the Board prescribes the procedure for computing the amount of the deficiency after the Board has heard and decided the issues raised and presented on the merits. Under the express provisions of this rule any hearing thereunder is confined to consideration of the correct computation of the deficiency or overpayment resulting from the report of the Board already made, and no argument is heard or consideration given to any new issue. Furthermore, by its express provisions the rule may not be taken as affording an opportunity for a rehearing or consideration. (Rule 50, *infra*, p. 42.)

The Board has held that new issues may not be raised and urged on a hearing under this rule. *Great Northern Ry. Co.*, 10 B. T. A. 1347, affirmed on other issues, 40 F. (2d) 372 (C. C. A. 8th), certiorari denied, 282 U. S. 855. It has also been sustained in the following cases: *O'Meara* v. *Commissioner*, 34 F. (2d) 390, 395 (C. C. A. 10th); *Boggs & Buhl* v. *Commissioner*, 34 F. (2d) 859, 861 (C. C. A. 3d); *Metropolitan Business College* v. *Blair*, 24 F. (2d) 176, 178 (C. C. A. 7th). Cf. *Sooy* v. *Commissioner*, 40 F. (2d) 634 (C. C. A. 9th). The rule is clearly a proper exercise of the power of the Board to prescribe rules of practice and procedure. The interests of orderly procedure demanded that petitioners present their contentions before the Board decided the case on the merits and denial of rehearing by the Board was clearly proper.

The contention which the petitioner sought to advance on rehearing was that if the annual allowances to the Coal Company for depletion are based upon the minimum royalty payments instead of upon the number of tons actually extracted it will be entitled to a larger depletion deduction than that determined by the respondent and approved by the Board. The Coal Company seeks to bring itself within the rule that the Government is contending for in *Murphy Oil Co.* v. *Burnet,* No. 80, October Term, 1932, which is to be argued just before this case. In that case the taxpayer, a lessor of oil property, received a bonus in connection with a lease, in addition to regular royalties stipulated in the lease.[7] The Government is contending that the bonus should be reported as gross income and a depletion allowance made in the same year, the bonus being considered as advance royalty for oil which the lessee has acquired the right to remove in the future. In that case the Government is seeking to uphold Treasury Regulations, which provide in substance that bonuses and minimum annual or advance royalties which are paid for the right to extract and remove mineral at any time thereafter shall be included in gross income and an allowance made for depletion of the value in

[7] Reference is made to the Government's brief in *Murphy Oil Co.* v. *Burnet.*

the ground to the lessor of the number of units of mineral so paid for in advance, and no further depletion is thereafter allowed on account of the extraction of such mineral so paid for in advance.[8] The Regulations further provide that, upon expiration, termination, or abandonment of the lease, the lessor shall restore to capital account any depletion deduction made in prior years on account of royalties or minerals paid for but not removed, and the amount so restored shall be included as income for the year in which the lease expires, terminates, or is abandoned.

Upon the facts disclosed in the present record it appears that the right of the lessees of the Coal Company to remove coal for minimum royalties subsequent to the year of payment was limited. There were six different leases of the Coal Company's property. (R. 42–43.) Only one, known as the "Cletus lease," was received in evidence.[9] (R. 85, 39–42.) This lease was offered as typical of the others. (R. 39–40, 85–86.) It provides that the lessee shall, among other things, have the exclusive privilege of mining and coking coal. The les-

[8] This is in accordance with Article 215 of Regulations 45 (1920 Edition), Article 216 of Regulations 62, and Article 216 of Regulations 65, as amended by T. D. 3938, V–2 C. B. 117 (*infra*, p. 40).

[9] This Coal Company proffered the other leases upon the hearing under Rule 50, in connection with its motion for rehearing, but the Board refused to receive them then. (R. 109–110.)

see agrees to pay 10 cents for each ton of coal mined and 15 cents for each ton of coke manufactured, and to pay as a minimum rental or royalty, $5,000 a year, whether the quantity of coal mined and coke manufactured shall produce that amount of royalty or not, but the lessee "shall have the privilege of mining the *next succeeding year,* free of royalty, a sufficient amount of coal above the amount necessary to produce the minimum royalty for that year to reimburse themselves for the deficiency in the preceding year." (Italics ours.) (R. 40–41.)

It is clear from the provision quoted that the payment of the minimum annual rental or royalties did not give to the lessees a right to mine at any time in the future a quantity of coal equal to the deficiency in the year of payment. The right was limited to the next succeeding year, and then only after the minimum quantity for that year had been mined It is, therefore, not covered by the terms of Article 215 of the Treasury Regulations. There was no continuing right in the lessee to remove coal in the future equal to the excess of the minimum payment over the total royalty at the per-ton rate for coal extracted. If the principle of the Regulation were applied to a case like the present, and depletion allowed on the basis of the minimum annual payments and the deficiency in tons of coal mined should not be removed in the following year, it would be necessary under the terms of the Regula-

tion to restore the excess depletion to capital account and to report it in income in the next succeeding year. Otherwise, the lessor would have been allowed depletion of his interest in the minerals where no depletion had taken place, either in fact or in theory.

But it appears from facts stipulated and found by the Board of Tax Appeals that the royalty payments on coal actually extracted was greater than the required annual minimum payments (except possibly for certain years in the case of one of the leases, and this depends upon one construction of the facts, as shown below).[10]

---

[10] These facts show:

Lease No. 1: Per ton royalty, 8 cents; annual minimum, $5,000. (R. 43.) In each year the tonnage mined and paid for exceeded the required minimum payment. (R. 44.)

Lease No. 2 (Cletus Mine): Per ton royalty, 10 cents; annual minimum, $5,000. (R. 41, 43.) The tonnage mined in each year was less than the annual payments actually received, which were uniformly $12,000. But the lease and the tabular statement in the finding of fact of the Board show that the required annual minimum payment is $5,000, and payments at the per ton rate for coal extracted in each year exceeded the latter amount. (R. 41, 43, 44.)

Lease No. 3: Per ton royalty, 7 cents; annual minimum, $4,000. (R. 43.) In each year the tonnage mined and paid for exceeded the required annual payment. (R. 45.)

Lease No. 4 (Warwick Mine and Exeter Mine): Per ton royalty, 10 cents; annual minimum, $10,000. (R. 43.) The amount mined and paid for at both mines always exceeded the annual minimum. If the minimum applies to each mine separately, in the case of the Warwick Mine there were three years in which the tonnage mined was less than the tonnage

From the references to the findings in Footnote 10, it is apparent that even if the Regulations were held to apply to leases with provisions for a very limited right of extraction to compensate for minimum royalty paid in excess of extraction, the facts disclose that there were no excess royalty payments under any of the leases, with one possible exception.[11]

---

that could be mined for the annual payment, but in only one case (1922) was the deficiency in tonnage mined (in part) in the following year. (R. 45.)

Lease No. 5: No required annual minimum payment.

Lease No. 6: This lease relates to an easement for hauling over the land of the Coal Company coal mined on property of others. It does not appear that it is an appropriate subject for depletion allowances.

[11] Whether or not there were excess payments in the case of this lease depends upon a construction of the facts. If the stated minimum annual royalty of $10,000 was the minimum for both of the mines grouped under Lease No. 4, there was no excess payment of royalty. If $10,000 was to be paid separately for each of the two mines, then there was an excess payment in the case of the Warwick Mine in three of the seven years involved, viz, 1920, 1921, and 1925; but only in 1922 was any coal mined to make up in part the deficiency of the preceding year. In the case of the Exeter Mine, under Lease No. 4, the receipts in each year exceeded $10,000, although they can not be reconciled with the figures of tonnage mined. (R. 45.)

We, therefore, submit that upon the facts in evidence it appears that (with possibly a minor exception in the case of one lease) the Coal Company would not in any event be entitled to a larger depletion allowance than that made to it by respondent, and thus denial of rehearing did not substantially prejudice it.

CONCLUSION

It is submitted that the decision of the court below should be affirmed.

Respectfully submitted.

THOMAS D. THACHER,
Solicitor General.
G. A. YOUNGQUIST,
Assistant Attorney General.
WHITNEY NORTH SEYMOUR,
SEWALL KEY,
ANDREW D. SHARPE,
Special Assistants to the Attorney General.

NOVEMBER, 1932.

APPENDIX

Constitution of the United States:

Article I

SEC. 9. * * *

No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken.

Sixteenth Amendment

The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1065, 1077:

SEC. 213. That for the purposes of this title (except as otherwise provided in section 233) the term "gross income"—

(a) Includes gains, profits, and income derived from * * *, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. The amount of all such items shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under subdivision (b) of

section 212, any such amounts are to be properly accounted for as of a different period; * * *

SEC. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

* * * * *

(9) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost including cost of development not otherwise deducted: *Provided,* That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: * * * such reasonable allowance in all the above cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee.

Revenue Act of 1921, c. 136, 42 Stat. 227, 237, 254:

SEC. 213 of the 1921 Act is substantially the same as Section 213 of the Revenue Act of 1918.

SEC. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

* * * * *

(9) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case, based upon cost including cost of development not

otherwise deducted: *Provided,* That in the case of such properties acquired prior to March 1, 1913, the fair market value of the property (or the taxpayer's interest therein) on that date shall be taken in lieu of cost up to that date: * * * such reasonable allowance in all the above cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee.

Revenue Act of 1924, c. 234, 43 Stat. 253, 267, 283:

SEC. 213 of the 1924 Act (U. S. C., Title 26, Sec. 954), is substantially the same as Section 213 of the Revenue Act of 1921.

SEC. 234. (a) In computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:

* * * * *

(8) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee. (U. S. C., Title 26, Sec. 986.)

Revenue Act of 1926, c. 27, 44 Stat. 9, 23, 41, 55, 116:

SEC. 213 of the 1926 Act (U. S. C. App., Title 26, Sec. 954), is substantially the same as Section 213 of the Revenue Act of 1924.

SEC. 234. (a) In computing the net income of a corporation subject to the tax im-

posed by section 230 there shall be allowed as deductions:

* * * * *

(8) In the case of mines, * * * a reasonable allowance for depletion and for depreciation of improvements, according to the peculiar conditions in each case; such reasonable allowance in all cases to be made under rules and regulations to be prescribed by the Commissioner with the approval of the Secretary. In the case of leases the deductions allowed by this paragraph shall be equitably apportioned between the lessor and lessee. (U. S. C. App., Title 26, Sec. 986.)

SEC. 274. (a) If in the case of any taxpayer, the Commissioner determines that there is a deficiency in respect of the tax imposed by this title, the Commissioner is authorized to send notice of such deficiency to the taxpayer by registered mail. Within 60 days after such notice is mailed (not counting Sunday as the sixtieth day), the taxpayer may file a petition with the Board of Tax Appeals for a redetermination of the deficiency. Except as otherwise provided in subdivision (d) or (f) of this section or in section 279, 282, or 1001, no assessment of a deficiency in respect of the tax imposed by this title and no distraint or proceeding in court for its collection shall be made, begun, or prosecuted until such notice has been mailed to the taxpayer, nor until the expiration of such 60-day period, nor, if a petition has been filed with the Board, until the decision of the Board has become final. Notwithstanding the provisions of section 3224 of the Revised Statutes the making of such assessment or the beginning of such proceeding or distraint during the time such prohibition is in force may be enjoined by a pro-

ceeding in the proper court. (U. S. C. App., Title 26, Sec. 1048.)

SEC. 1113. (a) Section 3226 of the Revised Statutes, as amended, is reenacted without change, as follows:

"SEC. 3226. No suit or proceeding shall be maintained in any court for the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or of any penalty claimed to have been collected without authority, or of any sum alleged to have been excessive or in any manner wrongfully collected until a claim for refund or credit has been duly filed with the Commissioner of Internal Revenue, according to the provisions of law in that regard, and the regulations of the Secretary of the Treasury established in pursuance thereof; but such suit or proceeding may be maintained, whether or not such tax, penalty, or sum has been paid under protest or duress. No such suit or proceeding shall be begun before the expiration of six months from the date of filing such claim unless the Commissioner renders a decision thereon within that time, nor after the expiration of five years from the date of the payment of such tax, penalty, or sum, unless such suit or proceeding is begun within two years after the disallowance of the part of such claim to which such suit or proceeding relates. The Commissioner shall within 90 days after any such disallowance notify the taxpayer thereof by mail."

(b) This section shall not affect any proceeding in court instituted prior to the enactment of the Revenue Act of 1924. (U. S. C. App., Title 26, Sec. 156.)

Treasury Regulations 45 (1920 Edition):

ART. 215. *Depletion—Adjustments of accounts based on bonus or advanced roy-*

alty.—(a) Where a lessor receives a bonus or other sum in addition to royalties, such bonus or other sum shall be regarded as a return of capital to the lessor, but only to the extent of the capital remaining to be recovered through depletion by the lessor at the date of lease. If the bonus exceeds the capital remaining to be recovered, the excess and all the royalties thereafter received will be income and not depletable. If the bonus is less than the capital remaining to be recovered by the lessor through depletion, the difference may be recovered through depletion deductions based on the royalties thereafter received. The bonus or other sum paid by the lessee for a lease made on or after March 1, 1913, will be his value for depletion as of date of acquisition.

(b) Where the owner has leased a mineral property for a term of years with a requirement in the lease that the lessee shall extract and pay for, annually, a specified number of tons, or other agreed units of measurement, of such mineral, or shall pay, annually, a specified sum of money which shall be applied in payment of the purchase price or royalty per unit of such mineral whenever the same shall thereafter be extracted and removed from the leased premises, the value in the ground to the lessor, for purposes of depletion, of the number of units so paid for in advance of extraction will constitute an allowable deduction from the gross income of the year in which such payment or payments shall be made; but no deduction for depletion by the lessor shall be claimed or allowed in any subsequent year on account of the extraction or removal in such year of any mineral so paid for in advance and for which deduction has once been made.

(c) If, for any reason, any such mineral lease shall be terminated or abandoned before the mineral which has been paid for in advance has been extracted and removed, and the lessor repossesses the leased property, the lessor shall adjust his capital accounts by restoring to the capital sum of the property the depletion deductions made in prior years on account of royalties on mineral paid for but not removed, and his income account shall be adjusted so as to include the amount so restored to capital sum as income of the year such lease is terminated or the property repossessed, and the tax thereon paid.

(d) Upon the expiration, termination, or abandonment of a lease, without the removal of any or all of the mineral contemplated by the lease, the lessor shall be required to restore to capital account so much of the bonus received and deducted from capital recoverable through depletion as is in excess of the actual depletion or loss in value sustained as a result of the operations under the lease and the corresponding amount will be income for the year in which the lease expires, terminates, or is abandoned.

Paragraphs (b) and (c) of the above article appear in the same form in Article 215 of Regulations 62, and Article 216 of Regulations 65 and 69, and in Article 236 of Regulations 74.

Paragraphs (a) and (d) originally appeared in the same form as above in Article 215 of Regulations 62 and Article 216 of Regulations 65, but were afterwards amended by T. D. 3938, V–2 C. B. 117, promulgated November 13, 1926, to read as follows (pp. 117–118):

Article 215 of Regulations 45 (1920 edition), article 215 of Regulations 62, and arti-

cle 216 of Regulations 65 are hereby amended to read as follows:

ART. 216 (215). *Depletion—Adjustments of accounts based on bonus or advanced royalty.*—(a) Where a lessor receives a bonus in addition to royalties, there shall be allowed as a depletion deduction in respect of the bonus an amount equal to that proportion of the cost or value of the property on the basic date which the amount of the bonus bears to the sum of the bonus and the royalties expected to be received. Such allowance shall be deducted from the amount remaining to be recovered by the lessor through depletion, and the remainder is recoverable through depletion deductions on the basis of royalties thereafter received.

(b) Where the owner has leased a mineral property for a term of years with a requirement in the lease that the lessee shall extract and pay for, annually, a specified number of tons, or other agreed units of measurement, of such mineral, or shall pay, annually, a specified sum of money which shall be applied in payment of the purchase price or royalty per unit of such mineral whenever the same shall thereafter be extracted and removed from the leased premises, the value in the ground to the lessor, for purposes of depletion, of the number of units so paid for in advance of extraction will constitute an allowable deduction from the gross income of the year in which such payment or payments shall be made; but no deduction for depletion by the lessor shall be claimed or allowed in any subsequent year on account of the extraction or removal in such year of any mineral so paid for in advance and for which deduction has once been made.

(c) If for any reason any such mineral lease shall be terminated or abandoned be-

fore the mineral which has been paid for in advance has been extracted and removed, and the lessor repossesses the leased property, the lessor shall adjust his capital accounts by restoring to the capital sum of the property the depletion deductions made in prior years on account of royalties on mineral paid for but not removed, and his income account shall be adjusted so as to include the amount so restored to capital sum as income of the year such lease is terminated or the property repossessed, and the tax thereon paid.

(d) Upon the expiration, termination, or abandonment of the lease, without the removal of any or all of the mineral contemplated by the lease, the lessor shall be required to restore to capital account the excess of the depletion theretofore allowable in respect of the bonus and royalty payments over the actual depletion or loss in value sustained as a result of the operations under the lease, and a corresponding amount must be returned as income for the year in which the lease expires, terminates, or is abandoned.

All rulings inconsistent herewith are hereby revoked.

Paragraphs (a) and (d) as thus revised appear in Article 216 of Regulations 69 and Article 236 of Regulations 74.

United States Board of Tax Appeals, Rule 50:

Settlement of final determination.—When the Board determines the issues in any proceeding and withholds final decision of the deficiency or overpayment for later computation, the parties shall, if they are in agreement as to the amount of the deficiency or overpayment, in accordance with the determination of the Board, file with the Board

an original and four copies of a computation showing the amount for entry of final decision forthwith. If the parties are not in agreement as to the amount to be entered in the final decision, either of them may file with the Board a computation of the deficiency or overpayment believed by him to be in accordance with the determination of the Board. The clerk will serve a copy thereof upon the opposite party and will thereupon place the matter upon the day calendar for hearing in due course and give the usual notice. If the opposite party fails to file objection, accompanied by an alternative computation, within five days prior to the date of such hearing, or any continuance thereof, the deficiency or overpayment shown in the computation already submitted shall be taken to be correct and decision thereon will be entered. If the parties submit different computations and amounts, they will be afforded an opportunity to be heard thereon on the date fixed, and the Board will determine the correct deficiency or overpayment and enter decision.

Any hearing under this rule will be confined strictly to the consideration of the correct computation of the deficiency or overpayment resulting from the determination already made, and no argument will be heard upon or consideration given to the issues or matters already disposed of by such determination or of any new issues. This rule is not to be regarded as affording an opportunity for rehearing or reconsideration.

U. S. GOVERNMENT PRINTING OFFICE: 1938

FILE COPY

MAY 24
CHARLES

No. 104

In the Supreme Court of the United States

OCTOBER TERM, 1932

BANKERS POCOHONTAS COAL COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

MEMORANDUM ON BEHALF OF THE COMMISSIONER IN OPPOSITION TO MOTIONS FOR REVIEW OF APPLICATION OF MANDATE AND RECALL OR MODIFICATION OF JUDGMENT AND MANDATE

In the Supreme Court of the United States

OCTOBER TERM, 1932

No. 104

BANKERS POCOHONTAS COAL COMPANY, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

MEMORANDUM ON BEHALF OF THE COMMISSIONER IN OPPOSITION TO MOTIONS FOR REVIEW OF APPLICATION OF MANDATE AND RECALL OF MODIFICATION OF JUDGMENT AND MANDATE

The respondent opposes the petitioner's motion filed herein on May 22, 1933, for the following reasons:

1. In its opinion herein, rendered December 5, 1932, the Court referred to the petitioner's contention that it was entitled to a different depletion allowance from that awarded by the Board of Tax Appeals because of the decision in *Murphy Oil Co.* v. *Burnet,* 55 F. (2d) 17 (C.C.A., 9th), affirmed, 287 U.S. 299,[1] and held, we believe, that the question was not properly presented by the record.

[1] The opinions of this Court in the instant case and in *Murphy Oil Co.* v. *Burnet*, *supra*, were rendered on the same date (December 5, 1932) and both were by Mr. Justice Stone.

Evidence upon this subject had been presented to the Board, for the first time, on an application for rehearing, but the Board had declined to consider it. This Court said:

> The purpose of the tendered evidence was to bring the case within the ruling of the Court of Appeals for the Ninth Circuit affirmed in No. 80, *Murphy Oil Company* v. *Burnet, supra,* that bonus payments to the lessor of a mineral lease are to be treated as advance payments of royalties and depletion allowed. This was a new issue. * * * It is not shown that the evidence tendered was not available to the petitioner in ample time to present it before the Board had made and filed its findings of fact and opinion. Under the circumstances, we cannot say that the Board abused its discretion in denying a rehearing.

2. The question of the applicability to this case of the decision of this Court in *Murphy Oil Co.* v. *Burnet, supra,* was presented to the Court in a petition for rehearing filed by the petitioner December 30, 1932, and denied January 9, 1933.

3. The present contention as to the application of what the petitioner conceives to be the rule approved by this Court in the *Murphy Oil Co. case* should not be considered, because it was not presented by assignments of error in the petition for certiorari herein, and apparently it was not presented to the Board or the Circuit Court of Appeals. In its petition for certiorari (p. 9) peti-

tioner specified as error the decision of the Board and the Circuit Court of Appeals:

> 4. In deciding that the excess amount of minimum payment received in any year from the grantee over the payment thereby made for coal actually mined within the year is not subject to any depletion allowance.

It appears from the statement of the proposed modification in the judgment and mandate of this Court (present motion, p. 9) that petitioner now seeks to have the excess of minimum annual payments over payments for coal mined in the various years treated as capital and not income, instead of having such excess subject to depletion allowance, which was the basis of its assignment of error quoted above. Aside from other objections to the motion, it seems to us that it would be improper to modify the judgment and mandate as requested and thereby to decide a question which was not properly presented to the Court when the case was here on the merits.

If the record properly presented the question which the petitioner now seeks to raise, and if it were presented *de novo* on the merits, we believe it could be demonstrated that the adjustment which the petitioner claims is not authorized by the decision of this Court in *Murphy Oil Co.* v. *Burnet, supra.* It would, however, unduly extended this memorandum to discuss the details of the adjustment and the application of the rule in the *Murphy*

Oil case thereto. In the absence of any indication that the form of the judgment or mandate was due to mistake or oversight, a new consideration of the merits in this respect seems quite out of place upon an application of this kind, and we believe that the Court should not be burdened with it at this stage of the proceedings.

The motion should be denied.

Respectfully submitted.

J. CRAWFORD BIGGS,
Solicitor General.

MAY 1933.

U. S. GOVERNMENT PRINTING OFFICE: 1 9

FILE COPY

DEC 30 19
CHARLES ELMORE C

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

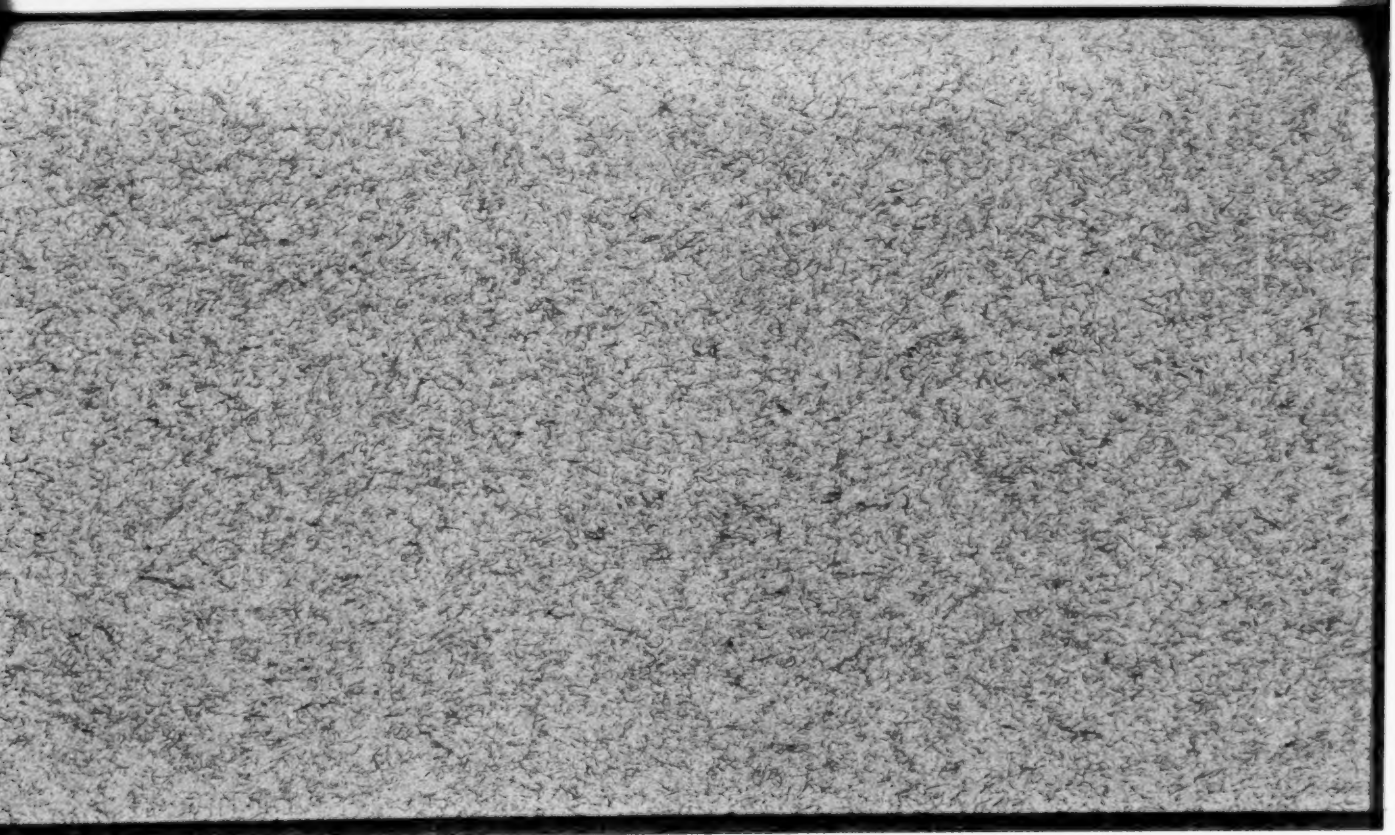
v.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

PETITION FOR REHEARING.
(Opinion December 5, 1932.)

CAMDEN R. McATEE,
Attorney for Petitioner.

MASON, SPALDING &
McATEE,
Of Counsel.



INDEX.

SUBJECT INDEX.

Page

Reconsideration and modification of *first* and *third* points decided, for cause:

a. Not responsive 1

b. Misapprehend the subject matter 1

c. Premises of fact are not those of the case 2

Additional facts pertinent:

No contract provision for minimum or maximum annual production 2

Receipts of royalties as bonus exceeded payment for coal mined 2

The error of the first point 3

Petitioner's propositions are:

a. The contract receipts contain no income increment 5

b. Depletion is not applicable where depletable interest, if any, ceased before the amendment 5

No calculable return from the contracts 6

Commissioner's depletion allowance is merely present value of royalty per ton, and conflicts with Reinecke v. Spalding, 280 U. S. 227, 233 6

Under facts, present value not existent, Burnet v. Logan, 283 U. S. 404, 413; Lucas v. Alexander, 279 U. S. 573, 579 7

Petitioner's rights vested before amendment may not be taken away by subsequent Revenue Acts .. 9

Amendment and Revenue Acts apply to subsequent transactions, according to Burnet v. Harmel, No. 26, November 7, 1932, which does not govern here. 9

The error of the third point:

Any depletion allowance should apply to the excess payments (Burnet v. Harmel and Murphy Oil Co. v. Burnet), but is here denied apparently because the necessary facts were not of record. The record shows the facts were in evidence and found by the Board. The Board reconsidered the case upon the issue of depletion upon *coal paid for* 13, 14

Page

Petitioner never asked review of the exclusion of the leases from evidence. It asked review of the refusal of depletion upon coal paid for respondent, in the Murphy Oil case, was asking the same thing, and here briefed and abandoned issue to avoid confession of error. The record substantiates the propriety of depletion allowances upon coal paid for..... 15

Conclusion 16

Decisions and authorities cited:

Burnet v. Harmel, No. 26, October Term, 1932, November 7, 1932..... 9, 13

Burnet v. Logan, 283 U. S. 404, 413..... 7

Lucas v. Alexander, 279 U. S. 573, 579..... 7

Murphy Oil Co. v. Burnet, No. 80, October Term, 1932, December 5, 1932..... 11, 13, 15

Reinecke v. Spalding, 280 U. S. 227, 233..... 6

Article 90, Regulations 45, 62, 65, 69..... 8

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE,
RESPONDENT.

PETITION FOR REHEARING.

Petitioner, after much reflection of counsel, respectfully requests a reconsideration and modification of the opinion herein (December 5, 1932, by Mr. Justice Stone) upon the first and third points decided, requiring their reversal in substance, for cause:

a. The decision is not responsive to the issues presented.

b. The decision seemingly misapprehends the subject matter in issue.

c. The decision is proper upon the premises of fact therein adopted—but said premises unfortunately do not reflect the case at bar.

The facts recited in the opinion[1] would be complete if they included the following additional but material details. First, *that the contracts called for no definite annual production of tonnage, either maximum or minimum*[1a], and second, *petitioner in the several years received royalties considerably in excess of the coal actually mined*[1b].

Out of these incidental but material details arises the case of petitioner, and without them its case upon

---

[1]The opinion states:

> "Petitioner, in 1912, acquired West Virginia coal lands in fee and, by assignment from the prior owners, certain leases or contracts entered into by them with various coal operators, by which the latter acquired the right to enter upon and use the lands for the production of coal and coke for a specified period, in consideration of stipulated royalties for the coal and coke produced, including minimum royalty payments in each year. In determining petitioner's income and profits taxes for the years 1920 to 1926, the Commissioner of Internal Revenue treated the royalty payments, after deducting a depletion allowance of 3.6¢ per ton of coal mined, as taxable income of petitioner, and assessed a corresponding increase in the tax."

[1a]R. p. 41.

[1b]See schedule, R. p. 160.

the first and third points decided is barren of the issues briefed and argued for petitioner in its presentation.

Assuming the presence of the two details of fact mentioned above, we briefly present our ground of objection to the decision.

The Error of the First Point as Decided.[2]

Petitioner does insist no part of the royalties is taxable income, but not because of any sale of coal in place or immediate passage of title. It does not argue the

---

[2] "*First.* It is insisted that no part of the royalties is taxable income of petitioner. Petitioner rests this contention on what is stated to be a rule of law of West Virginia, that under coal leases, like those presently involved, the title to the coal, in place, passes to the lessee or operator immediately on execution of the lease. From this it is argued that the royalties received were but payments for capital assets acquired and sold by petitioner before the adoption of the Sixteenth Amendment, and that their taxation as income is not authorized either by the statute or by the Sixteenth Amendment, because not apportioned.

"The question whether payments of bonus and royalties from the lessee to the lessor of an oil lease are income within the meaning of the revenue laws taxing income, or a return of capital as upon a sale of the oil, was recently before this Court in No. 26, *Burnet* v. *Harmel*, decided November 7, 1932. Although it was contended there, as it is here, that by state law the

royalties are but payments for capital assets acquired and sold by petitioner before adoption of the Amendment, because petitioner never sold the coal. It only acquired the land in 1912 after the coal was contracted

---

title to the mineral content of the leased land passed to the lessee upon execution of the lease, it was held that this characterization of the transaction in the local law did not affect the conclusion that the payments were gross income subject to tax, after the deductions allowed by the taxing act. The considerations which led to the conclusion that bonus and royalties paid to the lessor of Texas oil lands are taxable income and not a conversion of capital, as upon a sale of capital assets, are equally applicable to West Virginia coal leases, whether the title to the coal passes to the lessee in place at the date of the lease, or only upon severance by the lessee.

"The applicable statutes thus construed and applied do not tax any part of petitioner's capital investment before March 1, 1913. Section 234(*a*)(9) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, and regulations under it, require depletion allowances upon bonus and royalty payments received by the lessor of mineral lands, sufficient to provide for a return in full of his invested capital. The provisions of that section, and the related Treasury Regulations have been continued with the later Revenue Acts, see No. 80, *Murphy Oil Co.* v. *Burnet,* decided this day. The fact that the depletion allowance under the Revenue Act of 1913 was more limited is not pertinent here. *Burnet* v. *Thompson Oil & Gas Co.,* 283 U. S. 301."

in 1902, and also, in 1912, acquired the right to collect the subsequent contract payments. Sale of capital assets in place, or otherwise, or immediate passage of title, or their acquisition and sale either before or after the Amendment, these have nothing to do with the primary position of petitioner, that the receipts are the mere proceeds of a claim existing before the Amendment, and contain no income increment. They may and do touch the alternative issue of the pertinency of depletion allowances to the case. Petitioner insists the royalties are not depletable because the sale of coal in place with its immediate passage of title was effected before the enactment of the XVI Amendment, and petitioner never had a depletable interest.

Petitioner, under the typical contract, is entitled to 10 cents per ton of coal mined each year, and including a minimum payment of $5,000, and was entitled to that on March 1, 1913. How much will petitioner get thereafter in the unexpired 20 years of the 30 year term? It will be $100,000 theoretically of minimum, but the actual receipts beyond that depend on what the operator elects to produce. In fact, under the typical Cletus lease[3], receipts from 1908 to 1914, inclusive, were much less than $5,000 a year, and approximated the minimum in 1915-1917, and in 1918 and 1919 were double the contract minimum[3a]. In the later years they were $12,000 instead of $5,000, but much less coal was mined[3b]. No present value on the critical date

---

[3]R. pp. 40, 41.
[3a]R. p. 105.
[3b]R. p. 45.

can be assigned to such a contract. Lift it out of mining—if A says to B—"here's a dollar for the privilege of parking my car on your lot this month, and I will pay 25 cents every day I park there"—no one can calculate what B may make, or what the contract is worth to him—and the illustration is identical with the present case.

Will the present value of 3.6 cents per ton obtained by the Commissioner stand up under analysis? It is in effect $\frac{(14{,}000{,}000 \text{ ton x } 10 \text{ cents})}{14{,}000{,}000}$ *to present value*, which is the same as the present value of 10 cents at the beginning of 40 years. The Commissioner obtains this result indirectly under his regulations for computing depletion. He estimates 14,000,000 tons of content mineable at 350,000 tons per year, giving a 40 year life. He estimates 34,000 a year receipts for each of 40 years, or a total of $1,360,000, which at present value is $510,000. That divided by 14,000,000 tons is 3.6 cents per ton[4].

The mere present value of an ultimate receipt per ton is not the proper deduction according to *Reinecke* v. *Spalding*[5]. As here computed over a 40-year life of a contract, having but 20 years to run, it is in apparent

---

[4]R. p. 93.

[5]280 U. S. 227, 233—

> "—it disregards the fact that respondent's interest was in the mines considered as entireties and not in particular parts of ore beds which the lessee had agreed to remove during designated future years."

error, for it takes a larger present value at the beginning of 20 years than at the beginning of 40 years to realize 10 cents at the end of the periods. This Court has said a present value on the critical date is not computable in case of a mineral lease providing no minimum or maximum annual production nor payment in *Burnet* v. *Logan*[6]. It has further plumbed the situation in *Lucas* v. *Alexander*[7]. It is fully recognized the pro-

---

[6]283 U. S. 404, 413—

> "The lease contract did not require production of either maximum or minimum tonnage, or any definite payments. * * *
>
> "* * * a promise to pay indeterminate sums of money is not necessarily taxable income. 'Generally speaking the income tax law is concerned only with realized losses, as with realized gains.' "
>
> "The consideration for the sale was * * * the promise of future money payments wholly contingent upon facts and circumstances not possible to foretell with anything like fair certainty. The promise was in no proper sense equivalent to cash. It had no ascertainable fair market value."

[7]279 U. S. 573, 579 (Mr. Justice Stone, writing):

> "The purpose of ascertaining the value of the taxpayer's property on March 1, 1913, is as Par. 202 states, to measure that part of the total gain which has arisen or accrued after the enactment of any of the statutes taxing income and thus to arrive at his gain which may be taxed as income. Value of that date may be disregarded unless it serves that purpose. * * *—where

ceeds of a claim owned and existing on the critical date do not constitute income when subsequently collected[8].

> the property has no market value, the statute must be interpreted in the light of its purpose to ascertain taxable gains accruing since March 1, 1913. Hence, in such a case, its fair value on the critical date * * * must be taken * * * to be that part of the amount actually realized by the taxpayer, which, by the use of appropriate accounting methods, can fairly be said to have accrued before March 1, 1913—its value than as compared with the value in fact later realized by the taxpayer taken as a standard. * * * It is never necessary to speculate * * * as to what might later be realized from his property by the taxpayer, nor as to what might have been realized from his property by the taxpayer, nor as to what might have been realized if, on March 1, 1913, he had made some forced disposition of the property which would have precluded any taxable gain. For the necessity of ascertaining value as of March 1, 1913, can never arise until some later date when income has been produced by converting the property into money or money's worth and the amount actually realized is known, and then, as we have said, only for the purpose of apportioning the total gain which had accrued between the periods before and after March 1, 1913."

There is no accounting method which can appropriately be applied to the present case—for no annual return and no fixed term of years in which it will be certainly received can be evolved from the contract.

[8]Article 90, Regulations 45, 62, 65, 69. See Appendix to Petitioner's Brief, p. 51.

Here the contracts at issue were perfected and the resulting rights were vested prior to the XVI Amendment. Neither the XVI Amendment nor subsequent Revenue Acts are retroactive, and cannot decree that a sale of mineral in place was not effected in 1902. That they may do so and treat the parties as lessor and lessee entitled to depletion deductions in taxable transactions subsequent to the Amendment is the effect of *Burnet* v. *Harmel*[9]. Perhaps, the Court said this case was like the *Harmel* case in application of depletion deductions because the opinion herein says "the royalties received were but payments for capital assets acquired and sold by petitioner before the adoption of the XVI Amendment". In fact, the capital assets, if that mean the coal content, admittedly were never acquired or sold by petitioner, having been sold in place by its predecessor in 1902. As petitioner never had any interest in the coal content before the Amendment or thereafter, it would follow the statutory depletion allowances cannot be impressed upon petitioner concerning a coal content which it never owned, and in derogation of rights created and existing before the Amendment was enacted.

For these material reasons the principles of the *Harmel* case do not appear to govern this case, but are fully applicable to similar cases arising subsequent to the Amendment.

Summarizing, petitioner submits the opinion should decide whether the royalty receipts, collected by petitioner subsequent to the Amendment under the con-

---

[9]No. 26, Oct. Term, 1932, Nov. 7, 1932.

tracts previously effecting a sale of coal in place, are the non-taxable receipts of their claim therefor as existing on and before the critical date, and having no ascertainable capital value at that date. Alternatively, it should decide, in case of a sale of coal in place consummated before the Amendment, that the proceeds thereafter collected are not depletable under the subsequent Revenue Acts. However, this second statement is unnecessary if the first statement is deemed established.

The Error of the Third Point as Decided.[10]

If, under the first point, it appear there is no taxable income in the royalty receipts, the third point

---

[10] "*Third.* After the Board of Tax Appeals had filed its findings of fact and opinion, both respondent and petitioner submitted recomputations of the amount of the deficiency under the Board's report, as provided by Rule 50 of the Board's Rules of Practice. In petitioner's recomputation, the claim was made for the first time that the minimum royalty payments stipulated by the leases had in some instances exceeded the amount of the per ton royalty which would have been payable on actual production, and it was asked that the depletion allowance be computed upon the basis of the actual payments made, instead of upon the number of tons extracted. Petitioner, at a hearing on the recomputation, tendered evidence in support of this claim. The Board rejected the evidence and denied petitioner's motion for a rehearing

becomes of no importance, since it refers to the basis of depletion allowances.

The third point places petitioner outside the pale of *Burnet* v. *Harmel* and *Murphy Oil Co.* v. *Burnet*[11], with respect to allowance of depletion upon coal paid for but not mined. The facts in the opinion are substantially based upon those stated in the brief of defendant and vary from the record. This requires a brief explanation of the record.

---

[11]No. 80, Oct. Term, 1932, Dec. 5, 1932.

---

in order to present this contention. The Court below upheld this action.

"The Board is authorized to prescribe rules of practice and procedure for the conduct of proceedings before it. Par. 601, Revenue Act of 1928, c. 852, 45 Stat. 791, 871, 872, amending Par. 907(*a*), Revenue Act of 1924, as amended; see *Goldsmith* v. *Board of Tax Appeals*, 270 U. S. 117. Rule 50 prescribes the procedure for computing the amount of the deficiency after the Board has heard and decided the issues raised and presented on the merits. In terms, it directs that the hearing on the computation which it authorizes is to be 'confined strictly to the consideration of the correct computation of the deficiency or overpayment resulting from the determination already made, and no argument will be heard upon or consideration given to * * * any new issues'. The Board has held that under the Rule new issues may not be raised and urged on a hearing upon the computation. *Great Northern Ry. Co.* v. *Commissioner*, 10 B. T. A. 1347, affirmed on other issues

In trying the Board case, the parties proceeded upon the theory that 3.6 cents per ton had been allowed as depletion without stating whether the allowance was upon *coal paid for* or upon *coal mined*. In fact, the Commissioner was allowing depletion upon *coal paid for* in the deficiency letters[12]. The Board findings ex-

[12]R. pp. 31, 33, 35. The 1924, 1925 and 1926 depletion deduction as to the Superior P. C. Co. lease is upon 120,000 tons, although less than one-half was mined within the year. The same is true of the Oregon and Exeter leases, and others. Compare deficiency letters, *supra*, with Leases 2 and 4, R. pp. 44, 45, 160.

40 F. (2d) 372. The rule was a proper exercise of the power of the Board to prescribe the practice in proceedings before it. See *O'Meara* v. *Commissioner*, 34 F. (2d) 390, 395; *Boggs & Buhl* v. *Commissioner*, 34 F. (2d) 859, 861; *Metropolitan Business College* v. *Blair*, 24 F. (2d) 176, 178; compare *Sooy* v. *Commissioner*, 40 F. (2d) 634.

"The purpose of the tendered evidence was to bring the case within the ruling of the Court of Appeals for the Ninth Circuit affirmed in No. 80, *Murphy Oil Company* v. *Burnet*, *supra*, that bonus payments to the lessor of a mineral lease are to be treated as advanced payments of royalties and depletion allowed. This was a new issue. * * * It is not shown that the evidence tendered was not available to the petitioner in ample time to present it before the Board had made and filed its findings of fact and opinion. Under the circumstances, we cannot say that the Board abused its discretion in denying a rehearing."

hibited the quantities of coal paid for and coal mined each year and the amounts received as stipulated into evidence by the parties. The Board decided depletion was allowable only upon coal mined, following its previous decisions which declared any allowance of depletion upon coal paid for but not mined was improper, and which voided the regulation of respondent authorizing such allowance[13]. This position of the Board is now reversed in *Burnet* v. *Harmel* and *Murphy Oil Co.* v. *Burnet* (*supra*).

Thus, the Board decision created a new issue, not previously in controversy between the parties, and to be met in presentation of the respective Rule 50 tax computations. Respondent's computation, figured according to the Board opinion upon *coal mined*, was presented with verbal reservations[14]. Petitioner, in putting its computation forward upon *coal paid for*, urged a reopening of the case to effect an allowance upon *coal paid* for, pointing out that the schedules, already stipulated in evidence and incorporated in the findings of fact, showed the *coal paid for* substantially exceeded *coal mined* in the several years under some of

---

[13]R. p. 70.

[14]R. p. 108. Counsel for respondent stated * * * that this method was in accordance with the opinion of the Board in this case, and consistent with the Board's rulings in other cases, although the respondent in other cases was committed to the principle of allowing depletion on tonnage of coal paid for instead of upon tonnage of coal actually mined in a taxable year.

the leases[15], and offering the leases in further corroboration of the schedules.

Respondent urged receipt of the leases in evidence upon the propriety of a reopening, and only objected to their admission on the settlement issue, which objection was sustained[16].

The Board took the motion for reopening under advisement and subsequently overruled same[17].

The record thus discloses petitioner offered the leases as supplementing and confirming existing evidential facts stipulated by the parties and adopted by the Board, showing the actual receipt of payments for coal were excess of payments for coal mined in the several years, and that the Board reconsidered the case and subsequently denied a rehearing upon the issue whether depletion should be based upon *coal paid for* instead of merely upon *coal mined* within the year. It also discloses the issue of allowance upon *coal mined* instead of *coal paid for* first arose after the decision of the Board, but that evidence pertinent thereto was already of record.

Petitioner has never asked this Court to review the rejection of the leases. *The point is not assigned as*

---

[15]R. p. 109—

—"and offered to introduce said leases to substantiate the schedules, and to show said payment was the minimum royalty required to be paid under said leases."

[16]R. p. 110.

[17]R. pp. 69-70.

error and was not an issue before this Court. Petitioner did ask this Court to rule that its depletion was computable upon *coal paid for,* relying upon the schedules incorporated in the Board findings to show royalty receipts in excess payments for coal mined[18], were bonus payments subject to depletion. Respondent could not brief the question raised by petitioner without contradicting his position in the *Murphy Oil*[19] case, or admitting that bonus royalties are depletable, and hence, briefed the abandoned issue of admitting the leases in evidence.

Petitioner asks this Court to note that the present record showed by stipulation that the payments each year were much in excess of payments for coal actually mined within the year, and that the additional leases would only be corroborative and explanatory of an existing situation whereby the receipt of bonus payments was shown of record. The Court is asked now to conclude that petitioner is entitled to depletion upon

---

[18]Petitioner's Brief, p. 34—

> "The schedules in the Board findings as to Leases 2 and 4 show in the several years here in controversy, petitioner is deprived of $72,000 of depletition upon an excess of 2,000,000 tons paid for but not mined, and is required to taxpay said amount."

[19]While disallowing depletion upon bonus payments under this decision, the Commissioner by cross appeal in *Murphy Oil Co.* v. *Commissioner,* 55 F. (2) 17, sought and obtained a reversal of the same ruling therein.

the *coal paid for* each year and not merely upon *coal mined,* which is the present decision. The point represents $13,000 of taxes, exclusive of interest on same.

This motion for reconsideration seeks the following results:

1. That petitioner received no taxable income in the several years.
2. Alternatively, if it received taxable income including a capital return to be recaptured through the depletion allowances to a lessor, that said depletion allowance applies to *coal paid for* in the taxable years and not merely to coal mined within said years.
3. To avoid substantial injustice to petitioner by obtaining a proper correction of the opinion herein.

Respectfully submitted,

CAMDEN R. McATEE,
Counsel for Petitioner.

Certificate of Counsel.

The undersigned counsel for petitioner herein certifies that the foregoing petition for rehearing is presented in good faith and not for delay.

Respectfully,

CAMDEN R. McATEE,
Counsel for Petitioner.

FILE COPY

MAY 22

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

v.

COMMISSIONER OF INTERNAL REVENUE.

(Opinion December 5, 1932, by Mr. Justice Stone.)

MOTIONS ON BEHALF OF PETITIONER FOR REVIEW OF APPLICATION OF MANDATE AND FOR RECALL OR MODIFICATION OF JUDGMENT AND MANDATE HEREIN.

(Judgment, December 5, 1932; Mandate, January 11, 1933.)

SUPPORTING MEMORANDUM AND APPENDIX.

CAMDEN R. MCATEE,
Attorney for Petitioner.

SUBJECTS.

INDEX.

	Page
Motion	1
Jurisdiction	2
Question presented	2
Material facts	3
Substance of the record	7
Readjustment sought—its effect	9
Supporting memorandum:	
Procedure and jurisdiction	10
True intent and meaning of judgment and mandate	11
Bonus payment	14

APPENDIX.

Document.	*Subject Matter.*	
A–1.	Opinion of Supreme Court	16
A–2.	Judgment of Supreme Court	20
A–3.	Mandate of Supreme Court	21
A–4.	Board order on Circuit Court of Appeals mandate	23
A–5.	Petitioner's motion for entry of its recomputation	24
A–6.	Petitioner's recomputation	33
A–7.	Board order overruling motion and computation of petitioner	28
B.	Analysis of respective computations existing and proposed, using a simple illustration to show that net income received during life of property does not escape taxation, but that the allocation thereof to the several years is different	40

CITATIONS.

Bankers Pocahontas Coal Co. v. Commissioner, 18 B. T. A. 901, 55 F. (2) 626, 287 U. S. 308 ..... 25, 26

Board of Supervisors v. Kennicott, 4 Otto 498, 24 L. Ed. 260 32

Bramwell v. U. S. F. & G. Co., 269 U. S. 483, 489, 70 L. Ed. 368, 372 ..... 12, 30

Burnet v. Harmel, 287 U. S. 103, 112 ..... 15, 29

In re Burr, 4 Cr. 469, 481, 2 L. Ed. 684 12

Page

East Tennessee V. & G. R. Co. v. Interstate C. Com., 181 U. S. 1, 17, 45 L. Ed. 719, 725 ..... 13, 30
Ferguson v. Commissioner, 45 F. (2) 573, 577 ..... 15, 29
Himeley v. Rose, 5 Cranch 313 11
Illinois v. Illinois Cent. R. Co., 184 U. S. 77, 91, 46 L. Ed. 440, 447 11
Mitchel v. United States, 15 Pet. 52, 84, 10 L. Ed. 658, 670 .... 14, 33
Murphy Oil Co. v. Burnet, 287 U. S. 299, 55 F. (2) 17 ..... 2, 3, 34
Murphy Oil Co. v. Commissioner, 15 B. T. A. 1195 ..... 4, 5, 25
Nelson Land and Oil Co. v. Commissioner, 3 B. T. A. 315 25
Sibbald v. United States, 12 Pet. 488, 492, 9 L. Ed. 1167, 1169 .. 10
Story v. Livingston, 13 Pet. 358, 373, 10 L. Ed. 200, 207 ..... 12, 31
Thompson v. Maxwell Land Grant Co., 168 U. S. 451, 456, 42 L. Ed. 539 11
United States v. Mitchell, 271 U. S. 9, 14, 70 L. Ed. 799, 802 .... 13, 31
West v. Brashear, 14 Pet. 51, 54, 10 L. Ed. 350, 351 31

Article 204 (d), Reg. 45, 62, 65, 69 ..... 8, 29

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104

BANKERS POCAHONTAS COAL COMPANY,
PETITIONER,

vs.

COMMISSIONER OF INTERNAL REVENUE.

(Opinion December 5, 1932, by Mr. Justice Stone.)

MOTIONS ON BEHALF OF PETITIONER FOR REVIEW OF APPLICATION OF MANDATE AND FOR RECALL OR MODIFICATION OF JUDGMENT AND MANDATE HEREIN.

Petitioner, Bankers Pocahontas Coal Company, by its attorney, respectfully moves the Court for

Review of the application by the United States Board of Tax Appeals of the mandate herein, and

For any necessary recall or modification of its judgment or mandate, or both, as may appear necessary to do justice between the parties.

For Cause.

In support hereof petitioner respectfully would show:

Jurisdiction.

Said mandate issued in the present term, to wit, on January 11, 1933. (Appendix A-3.)

The Present Record.

In supplement to the original record, petitioner here presents (Appendix) (A-1) the opinion, (A-2) the judgment and (A-3) the mandate of this Court; (A-4) Board order reciting the mandate of the Circuit Court of Appeals, (A-5) petitioner's motion filed before the Board for entry of tax determination under the mandate, (A-6) petitioner's proposed determination, and (A-7) Board decision overruling petitioner's motion and proposed determination. The copies of the Board records are certified by its Clerk to be true and correct.

The Questions Here Presented.

Whether, it appearing this Court omitted the question in its opinion herein, the resulting general affirmance is intended to deny petitioner the benefit of the principles originally applied by the respondent Commissioner, and approved by this Court in *Murphy Oil Co.* v. *Burnet,* before decision of this instant case,

to wit: that bonus payments are capital returns which reduce subsequent depletion allowances. Petitioner does not attempt to question any point decided in the opinion of this Court herein, only contending it should justly have the benefit of said principles upon the facts of record.

The Material Facts.

The order granting certiorari as entered on October 10, 1932, provided:

> * * * "the case is assigned for argument immediately following Case No. 80, *Murphy Oil Co.* v. *Burnet,* Commissioner of Internal Revenue."

The petition for certiorari presented as a ground therefor (pp. 9, 26):

> "The Board and Court below erred (references to opinion of each):
>
> "4. In deciding that the excess amount of minimum payment received in any year from the grantee over the payment thereby made for coal actually mined within the year is not subject to any depletion allowance (R., pp. 49, 134)."
>
> "*Reason* 2. *An important question of federal taxation is decided in a way in direct conflict with a decision of another Circuit Court of Appeals.*
>
> "*Question:*
>
> "2(*b*). *Whether the excess amount of minimum payment received in any year from the grantee over the payment thereby made for coal actually mined within the year is subject to any depletion allowance.*"

Responsive to the opposition filed against said petition, petitioner stated (p. 10):

> "Respondent (Opposition, p. 15), entirely misconceived any alleged conflict of the present case with the *Murphy Oil Company* case, wherein the Circuit Court of Appeals held a cash bonus was subject to depletion allowances and reversed the Board rulings which the Court of Appeals herein has sustained. Petitioner Coal Company here received the minimum annual payment as a cash bonus to the extent that the operator could not mine coal equal to such payment, and upon this ground, affirmed by the lower Court (R., p. 132), that such excess cash payment is a bonus, not being a payment for coal actually mined, depletion on such bonus is herein denied (R., p. 49). That makes the present case identical with the *Murphy Oil* case in which certiorari has been allowed."

In the Murphy Oil Company Appeal (15 B. T. A. 1195) and herein (18 B. T. A. 901), the Board held bonus payments were gross income not subject to depletion on the ground that the Bureau regulations providing for depletion thereof were invalid. Upon cross petition to the Circuit Court of Appeals, Ninth Circuit, taken by respondent Commissioner in the *Murphy Oil Company* case, the Board was reversed and this Court, in affirming the Circuit Court of Appeals, says of the Commissioner's action under the original and amended regulations:

> * * * "the requirements of the amended regulation were satisfied by treating the whole bonus as a return of capital, and deducting from

> the depletion alowance on each barrel of the royalty oil the proportion of the capital investment already returned by the bonus. This is what the Commissioner did. * * * Stated in another way, the total amount of the bonus was deducted from petitioner's total capital investment in oil in the ground returnable by depletion allowances, with a corresponding reduction in the per barrel capital investment in the oil reserve. Thus the Commissioner treated the whole of the bonus as a return, in advance of abstraction of the oil, as a part of the petitioner's capital investment in the oil in the ground, with which it would part, in a technical legal sense, only upon abstraction. In consequence, the deduction for depletion allowed on royalties received in 1919 and 1920 was reduced; * * *
>
> "But the regulation does not require him (the Commissioner) to make estimates which are unreasonable, for where none can be made with reasonable accuracy the Commissioner cannot find that the 'sum of the bonus and royalties expected to be received' exceeds the capital investment. In that event the whole of the bonus will be treated, as in this case, as a return."

In this Bankers case, upon petitioner's petition for review, the Circuit Court of Appeals, Fourth Circuit, did not pass upon the bonus point, and its general affirmance of the Board placed its decision in conflict with the *Murphy Oil Company* case decided by the Ninth Circuit.

This Bankers case was argued in this Court immediately following the *Murphy Oil Company* case, and

was decided immediately after decision of that case on December 5, 1932, both opinions being by Mr. Justice Stone, who said in the opinion herein:

> "We granted certiorari on a petition which assails the judgment below on three grounds, which will be separately considered."

However, the opinion (Appendix A-1), entirely omits the point of depletable bonus, and thereby same is not decided of record. After said opinions, the two cases stand in conflict upon the point as they did after the decisions of the respective Circuit Court of Appeals and before they entered this Court.

A request for rehearing by petitioner was thereafter filed and denied.

The judgment of this Court (December 5, 1932; Appendix A-2), is that the Circuit Court of Appeals be affirmed.

Its mandate thereon (January 11, 1932; Appendix A-3) recites the judgment of the lower court, and that same is affirmed, and orders remand of the case, commanding:

> • • • "that such proceedings be had in said cause, as according to right and justice, and the laws of the United States, ought to be had, the said writ of certiorari notwithstanding."

From the Circuit Court of Appeals its mandate issued and was received by the Board of Tax Appeals. Whereupon the Board (January 13, 1933—Appendix A-4), ordered the parties to present recomputations only for the year 1924.

The recomputation tendered by respondent Commissioner for said year 1924, gave effect only to the

point reversed, and, being to that extent correct, is not herein material in its details and is omitted.

With tender of its recomputation for all the years, petitioner presented its motion that said recomputation be entered as a proper application and construction of the mandate under the principles of the *Murphy Oil Company* case as applicable thereto (Petitioner's motion, Appendix A-5) (Petitioner's recomputation, Appendix A-6).

Thereupon, the Board overruled and denied the motion and rejected the proposed recomputation of petitioner and entered its order redetermining the 1924 tax in the amount proposed by respondent Commissioner, and thereby followed said mandate as not ambiguous (May 19, 1933, Appendix A-7).

Wherefore, this motion is the result.

The Substance of the Record.

The redetermination proposed by petitioner rests entirely upon matters of record, and purposes a correction of the Board determination as justified by the principles of the *Murphy Oil Company* case.

From the findings of fact by the Board, the following material facts appear:

(*a*) Under the contracts of 1902 petitioner received in the subsequent years including those in controversy a fixed sum per ton of coal mined ($0.10 usually), and a further fixed sum—

> * * * "during the continuance of this lease, as a minimum rental or royalty, whether the quantity of coal mined shall produce that amount of royalty or not, but the lessees shall have the privilege of mining the next succeeding

year, free of royalty a sufficient amount of coal above the amount necessary to produce the minimum royalty for that year to reimburse themselves for the deficiency in the preceding year" (Record p. 41).

(*b*) Petitioner had on March 1, 1913, recoverable coal computable as 37,608,642 tons (R. p. 43) of a capital value of $1,353,911.11 (R. pp. 53, 128).

NOTE.—In case of a lessor with property leased on March 1, 1913, as herein the basic capital subject to depletion is the value on the basic date of the expected royalties (Reg. 45, 62, 65, 69; Article 204 (*d*)). Assuming bonus payments may be expected under the lease-contract, same and the expected royalties cannot be determined or expected with reasonable accuracy as together exceeding the invested capital or basic value, and the actual method of the *Murphy Oil Company* case is applicable, treating the bonus as a return of capital effecting a decrease of the subsequent depletion unit deduction.

(*c*) The tonnage mined and the receipts for 1913 and through 1919, appear whereby the existing capital value on January 1, 1920, is directly computable (R. p. 44).

(*d*) The tonnage mined, the receipts and the tonnage paid for is scheduled as to each lease, a typical schedule being (R. p. 44):

Year.	Tonnage mined.	Paid for.	Receipts.	Comment—Bonus.
1920	57,189	120,000	$12,000	$6,281.10
1921	54,660	120,000	12,000	6,534.00
1922	55,864	120,000	12,000	6,413.60
1923	51,422	120,000	12,000	6,847.80
1924	57,928	120,000	12,000	6,207.20
1925	68,804	120,000	12,000	5,119.60
1926	90,029	120,000	12,000	2,992.10

It appearing 120,000 tons were paid for at 10 cents per ton, or $12,000, and that, in 1920, 57,189 tons were mined, there remain 62,811 tons not extracted, or $6,281.10 as a bonus payment. The column, "Comment —Bonus," above, is here inserted as a statement of the bonus each year, and it is equally easy of computation in the other lease-schedules.

The Readjustment Sought and Its Effect.

Petitioner contends, the bonus being apparent each year, same is a return of capital used to reduce the invested capital and thereby the resulting depletion unit for the succeeding year or years. The effect does not disturb the total of taxable income derived from the property. An illustration is attached (Appendix B).

The readjustment sought is amendment of the judgment and mandate by adding thereto the following words or their substance:

> * * * "is affirmed, excepting as modification thereof is necessary to return to petitioner the minimum annual payments as capital and not as income to the extent they may exceed payments for coal mined in the year as decided in *Murphy Oil Company* v. *Burnet* by this Court."

Further reasons are given as argument in the annexed memorandum.

Respectfully,

CAMDEN R. MCATEE,
Attorney for Petitioner.

Supporting Memorandum.

ARGUMENT.

Procedure and Jurisdiction.

The mandate herein being that the lower court is "*affirmed*", said lower court is bound thereby.

> "The inferior court is bound by the decree as the law of the case, and must carry it into execution according to the mandate. They cannot vary it, or examine it for any other purpose than execution, or give any other or further relief, or review it upon any matter decided upon appeal for error apparent, or intermeddle with it, further than to settle so much as has been determined."
>
> *Sibbald* v. *United States*, 12 Pet. 488, 492, 9 L. Ed. 1167, 1169.

It follows in neither the Circuit Court of Appeals nor Board of Tax Appeals by any proceedings therein, could the previous determination of the Board be changed, and that appeal or other steps taken therein to return the case to the Supreme Court, under such circumstances, are superfluous.

The *Sibbald* opinion, *supra*, recognizes this in that therein this Court acted upon a petition and motion for issue of a revised mandate giving proper execution to the decree.

The *Sibbald* opinion, *supra*, is further authority for the proposition that a Court cannot reverse or annul its own final decrees or judgments for errors of fact or law, after the term in which they have been rendered,

unless for clerical mistakes, or to reinstate a cause dismissed by mistake.

The judgment and mandate herein were entered in the present term.

In a long series of decisions beginning probably with *Himely* v. *Rose,* 5 Cranch 313, and as approved in *Illinois* v. *Illinois Cent. R. Co.,* 184 U. S. 77, 91; 46 L. Ed. 440, 447, it is held that none of the questions originally before the Court can be reheard or decided. The rule is succinctly stated in *Thompson* v. *Maxwell Land Grant Co.,* 168 U. S. 451, 456, 42 L. Ed. 539, as:

> "It is the settled law of this Court, as of others, that whatever has been decided upon one appeal or writ of error cannot be reexamined on a second appeal or writ of error brought in the same suit. The first decision has become the settled law of the case."

Admitting these propositions, it remains that this Court may properly inquire into the execution of its mandate, for as said by Chief Justice Marshall in the argument of *Himely* v. *Rose, supra:*

> "Nothing is before this court but what is subsequent to the mandate."

and he begins his opinion, saying:

> "A decree having been formerly rendered in this cause, the Court is now to determine whether that decree has been executed according to its true intent and meaning."

The True Intent and Meaning.

The judgment and mandate flow from the opinion. The opinion herein sets up and considers three specific

grounds on which, it is said, certiorari was granted. But the third point set up and considered is not the point of bonus payments as affected by the Murphy Oil Company case, and upon the points set up and considered, the Murphy Oil case is not relevant.

Knowing in *Bramwell* v. *U. S. F. & G. Co.*, 269 U. S. 483, 489, 70 L. Ed. 368, 372, this Court has said:

> "It is a general rule of universal application that general expressions used in a court's opinion are to be taken in connection with the case under consideration."

we come naturally to the proposition in *Story* v. *Livingston*, 13 Pet. 358, 373, 10 L. Ed. 200, 207, that

> "The mandate is to be interpreted according to the subject matter to which it has been applied, and not in a manner to cause injustice."

The case under consideration, as stated in the opinion, not being inclusive of the *Murphy Oil Company* issue, it is reasonably submitted that a judgment and mandate effecting an affirmance in conflict with the *Murphy Oil Company* case was not intended.

In the case, *In re Burr*, 4 Cr. 469, 2 L. Ed. 684, an opinion of the Supreme Court is extensively discussed. First it is said:

> "Every opinion, to be correctly understood, ought to be considered with a view to the case in which it was delivered" (p. 481).

That case, stated in the present opinion does not include the bonus payments. Next the *Burr* opinion proceeds:

> "The opinion of a single judge certainly weighs as nothing if opposed to that of the Supreme Court; but if he was one of the judges who assisted in framing that opinion, if while the impression under which it was framed was yet fresh in his mind, he delivered an opinion on the same testimony, not contradictory to that which had been given by all the judges together, but showing the sense in which he understood terms that might be differently expounded, it may fairly be said to be in some measure explanatory of the opinion itself."

There is no contradiction in the opinion herein of the opinion in the *Murphy Oil Company* case, until we come to the judgment and mandate, and that such contradiction is not intentional seems apparent. Without intentional contradiction the point contradicted herein is not foreclosed and correction of the judgment and mandate will sufficiently adjust the matter.

In *United States* v. *Mitchell,* 271 U. S. 9, 14, 70 L. Ed. 799, 802, it is said:

> "It is not to be thought that a question not raised by counsel or discussed in the opinion had been decided merely because it existed in the record and might have been raised and considered."

In *East Tennessee V. and G. R. Co.* v. *Interstate C. Com.,* 181 U. S. 1, 17, 45 L. Ed. 719, 725, concerning the construction to be given to its opinions, the Court says:

> "The language of the opinions which is relied upon must be read in connection with its con-

> text, and must be construed in the light of the issue which was in controversy in the cases and which was decided."

Conceding counsel attempted to raise the bonus issue herein, and this Court in granting certiorari inferentially recognized its existence, it yet remains the opinion omits the question, and is decisive that it is not *"the issue which was in controversy in the cases and which was decided"*, quoting from the *East Tennessee* case, *supra.*

In conclusion, reference is made to authorities in the motion before the Board (Appendix A-5), and particularly to *Mitchell* v. *United States,* 15 Pet. 52, 84; 10 L. Ed. 658, 670, wherein it is said:

> "The meaning of the mandate may be ascertained from the instrument itself; but the reasons which induced the Court to make it, are to be found in the evidence contained in the original record. The Court will now do what it did in the case of Sibbald (12 Pet. 483). It said:
>
> " 'To ascertain the true intention of the decree and mandate of this Court, the decree of the court below, and of this Court, and the petitioner's title, must be taken into consideration. In 10 Wheat. 431, this Court says: "The proceedings in the original suit are always before the Court, so far as to determine any new points between the parties".' "

The Bonus Payments.

The effect of the leases herein is to create a bonus payment, notwithstanding the receipts are termed rentals or royalties. A royalty is the retained inter-

est of the lessor received as revenue (*Ferguson* v. *Commissioner*, 45 F. (2) 573, 577), and this Court says same is measured by actual production (*Burnet* v. *Harmel*, 287 U. S. 103, 112). The payment herein in excess of payment for actual production is not a royalty within these definitions. It is not a rental for it may be entirely absorbed by production, in which case it is a royalty and not a rental, and, therefore, if not absorbed, it remains and is a mere premium or bonus.

Respectfully submitted,

CAMDEN R. MCATEE,
Attorney for Petitioner.

APPENDIX A-1.

SUPREME COURT OF THE UNITED STATES.

No. 104.

BANKERS POCAHONTAS COAL COMPANY

vs.

COMMISSIONER OF INTERNAL REVENUE.

On Writ of Certiorari to the Circuit Court of Appeals for the Fourth Circuit.

Dec. 5, 1932.

Mr. Justice STONE delivered the opinion of the court.

Petitioner, in 1912, acquired West Virginia coal lands in fee and, by assignment from the prior owners, certain leases or contracts entered into by them with various coal operators, by which the latter acquired the right to enter upon and use the lands for the production of coal and coke for a specified period, in consideration of stipulated royalties for the coal and coke produced, including minimum royalty payments in each year. In determining petitioner's income and profits taxes for the years 1920 to 1926, the Commissioner of Internal Revenue treated the royalty payments, after deducting a depletion allowance of 3.6 cents per ton of coal mined, as taxable income of petitioner, and assessed a corresponding increase in the tax. On appeal this ruling of the Commissioner was sustained, both by the Board of Tax Appeals, 18 B. T. A. 901, and the Court of Appeals for the Fourth Circuit, 55 F. (2) 626. We granted certiorari, — U. S. —, on a petition which assails the judgment below on three grounds, which will be separately considered.

First. It is insisted that no part of the royalties is taxable income of petitioner. Petitioner rests this contention on what is stated to be a rule of law of West Virginia, that under coal leases, like those presently involved, the title to the coal, in place, passes to the lessee or operator immediately on execution of the lease. From this it is argued that the royalties received were but payments for capital assets acquired and sold by petitioner before the adoption of the Sixteenth Amendment, and that their taxation as income is not authorized either by the statute or by the Sixteenth Amendment, because not apportioned.

The question whether payments of bonus and royalties from the lessee to the lessor of an oil lease are income within the meaning of the revenue laws taxing income, or a return of capital as upon a sale of the oil, was recently before this Court in No. 26, *Burnet* v. *Harmel,* decided Nov. 7, 1932. Although it was contended there, as it is here, that by State law the title to the mineral content of the leased land passed to the lessee upon execution of the lease, it was held that this characterization of the transaction in the local law did not affect the conclusion that the payments were gross income subject to tax, after the deductions allowed by the taxing act. The considerations which led to the conclusion that bonus and royalties paid to the lessor of Texas oil lands are taxable income and not a conversion of capital, as upon a sale of capital assets, are equally applicable to West Virginia coal leases, whether the title to the coal passes to the lessee in place at the date of the lease, or only upon severance by the lease.

The applicable statutes thus construed and applied do not tax any part of petitioner's capital investment before March 1, 1913. Section 234 (*a*) (9) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, and regulations under it, require depletion allowances upon

bonus and royalty payments received by the lessor of mineral lands, sufficient to provide for a return in full of his invested capital. The provisions of that section, and the related Treasury Regulations have been continued with the later revenue acts, see No. 80, *Murphy Oil Co.* v. *Burnet*, decided this day. The fact that the depletion allowance under the Revenue Act of 1913 was more limited is not pertinent here. *Burnet* v. *Thompson Oil & Gas Co.*, 283 U. S. 301.

Second. In a suit brought by the petitioner in the District Court for Northern West Virginia, *Bankers Pocahontas Coal Co.* v. *White*, Collector of Internal Revenue, with respect to taxes for the years 1914 to 1919, it was held that petitioner was entitled to a depletion allowance on royalties received from the leases involved in the present suit, of 5¢ per ton of coal mined. It is insisted that the decision in that case was *res adjudicata* of that issue, and that in fixing the depletion allowance of the present case at 3.6¢ per ton, the court below and the Board of Tax Appeals erroneously refused to follow the decision of the district court in the earlier case. With respect to this contention it is sufficient to say that the suit in the district court was not against the Commissioner of Internal Revenue, the respondent here, but against the Collector, judgment against whom is not *res adjudicata* against the Commissioner or the United States. *Graham & Foster* v. *Goodcell*, 282 U. S. 409, 430; *Sage* v. *United States*, 250 U. S. 33; see *Smietanka* v. *Indiana Steel Co.*, 257 U. S. 1; compare *Union Trust Co.* v. *Wardell*, 258 U. S. 537.

Third. After the Board of Tax Appeals had filed its findings of fact and opinion, both respondent and petitioner submitted recomputations of the amount of the deficiency under the Board's report, as provided by Rule 50 of the Board's Rules of Practice. In petitioner's recomputation, the claim was made for the

first time that the minimum royalty payments stipulated by the leases had in some instances exceeded the amount of the per ton royalty which would have been payable on actual production, and it was asked that the depletion allowance be computed upon the basis of the actual payments made, instead of upon the number of tons extracted. Petitioner, at a hearing on the recomputation, tendered evidence in support of this claim. The Board rejected the evidence and denied petitioner's motion for a rehearing in order to present this contention. The court below upheld this action.

The Board is authorized to prescribe rules of practice and procedure for the conduct of proceedings before it. Section 601, Revenue Act of 1928, c. 852, 45 Stat. 791, 871, 872, amending Section 907 (*a*), Revenue Act of 1924, as amended; see *Goldsmith* v. *Board of Tax Appeals*, 270 U. S. 117. Rule 50 prescribes the procedure for computing the amount of the deficiency after the Board has heard and decided the issues raised and presented on the merits. In terms, it directs that the hearing on the computation which it authorizes is to be "confined strictly to the consideration of the correct computation of the deficiency or overpayment resulting from the determination already made, and no argument will be heard upon or consideration given to * * * any new issues". The Board has held that under the rule new issues may not be raised and urged on a hearing upon the computation *Great Northern Ry. Co.* v. *Commissioner*, 10 B. T. A. 1347, affirmed on other issues 40 F. (2d) 372. The rule was a proper exercise of the power of the Board to prescribe the practice in proceedings before it. See *O'Meara* v. *Commissioner*, 34 F. (2d) 390, 395; *Boggs & Buhl* v. *Commissioner*, 34 F. (2d) 859, 861; *Metropolitan Business College* v. *Blair*, 24 F. (2d) 176, 178; compare *Sooy* v. *Commissioner*, 40 F. (2d) 634.

The purpose of the tendered evidence was to bring the case within the ruling of the Court of Appeals for the Ninth Circuit affirmed in No. 80, *Murphy Oil Company* v. *Burnet, supra,* that bonus payments to the lessor of a mineral lease are to be treated as advanced payments of royalties and depletion allowed. This was a new issue. We need not consider the contention of the Government that it does not clearly appear either that the stipulated minimum payments exceeded the total per ton royalties upon the leases or that, even if they did, the excess of the minimum royalties over the royalties computed on actual production can, upon a proper construction of the leases, be treated as advance payment of the per ton royalties to accrue in future years. It is not shown that the evidence tendered was not available to the petitioner in ample time to present it before the Board had made and filed its findings of fact and opinion. Under the circumstances, we cannot say that the Board abused its discretion in denying a rehearing.

Affirmed.

APPENDIX A-2.

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1932.

No. 104

BANKERS POCAHONTAS COAL COMPANY, *Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Fourth Circuit.

This cause came on to be heard on the transcript of the record from the United States Circuit Court of

Appeals for the Fourth Circuit, and was argued by counsel.

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the said United States Circuit Court of Appeals, in this cause, be, and the same is hereby, affirmed; and that this cause be, and the same is hereby, remanded to the said Circuit Court of Appeals.

Per Mr. Justice STONE,
December 5, 1932.

APPENDIX A-3.

UNITED STATES OF AMERICA, *ss:*

[SEAL.]

The President of the United States of America to the Honorable the Judges of the United States Circuit Court of Appeals for the Fourth Circuit, Greeting:

Whereas, lately in the United States Circuit Court of Appeals for the Fourth Circuit, in a cause between Bankers Pocahontas Coal Company, Petitioner, and Commissioner of Internal Revenue, Respondent, No. 3215, wherein the judgment of the said Circuit Court of Appeals, entered in said cause on the 27th day of January, A. D. 1932, is in the following words, viz.:

"This cause came on to be heard on the transcript of the record from the United States Board of Tax Appeals, and was argued by counsel.

On Consideration Whereof, It is now here ordered and adjudged by this Court that the decision of the said Board of Tax Appeals, in this cause, be, and the same is hereby, affirmed except as to the determination of the deficiencies of the corporation for the year 1924, and as to this year, this cause be, and the same is hereby, remanded to the United States Board of Tax

Appeals for further proceedings in accordance with the opinion of the Court filed herein.

January 27, 1932.

MORRIS A. SOPER,
U. S. Circuit Judge."

as by the inspection of the transcript of the record of the said United States Circuit Court of Appeals which was brought into the Supreme Court of the United States by virtue of a writ of certiorari agreeably to the act of Congress, in such case made and provided, fully and at large appears.

And whereas, in the present term of October, in the year of our Lord one thousand nine hundred and thirty-two, the said cause came on to be heard before the said Supreme Court, on the said transcript of record, and was argued by counsel;

On consideration whereof, It is now here ordered and adjudged by this Court that the judgment of the said United States Circuit Court of Appeals in this cause be, and the same is hereby, affirmed.

And it is further ordered, That this cause be, and the same is hereby, remanded to the said Circuit Court of Appeals.

December 5, 1932.

You, therefore, are hereby commanded that such proceedings be had in such cause, as according to right and justice, and the laws of the United States, ought to be had, the said writ of certiorari notwithstanding.

Witness, the Honorable Charles E. Hughes, Chief Justice of the United States, the eleventh day of January, in the year of our Lord one thousand nine hundred and thirty-three.

(Signed) CHARLES ELMORE CROPLEY,
Clerk of the Supreme Court
of the United States.

[Endorsed:] File No. 36,801. Supreme Court of the United States, No. 104, October Term, 1932. Bankers Pocahontas Coal Company vs. Commissioner of Internal Revenue. Mandate.

APPENDIX A-4.

UNITED STATES BOARD OF TAX APPEALS.

WASHINGTON.

Docket No. 42664.

BANKERS POCAHONTAS COAL CO., *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

ORDER.

(Entered May 19, 1933)

The petitioner having prosecuted an appeal to the Circuit Court of Appeals for the Fourth Circuit from the decision of the Board in the above-entitled proceeding entered July 16, 1930, and that court having on January 13, 1933, issued a mandate directed to this Board, reading in part as follows:

> " * * * It is now here ordered and adjudged by this Court that the decision of the said Board of Tax Appeals, in this cause, be, and the same is hereby, affirmed except as to the determination of the deficiencies of the corporation for the year 1924, and as to this year, this cause be, and the same is hereby, remanded to the United States Board of Tax Appeals for further proceedings in accordance with the opinion of the Court filed herein. January 27, 1932."

It is hereby

Ordered that the parties litigant file with this Board, on or before March 1, 1933, recomputations of the deficiency for 1924 in accordance with the opinion of the Circuit Court of Appeals entered January 27, 1932, and the proceeding is hereby set down for hearing on the Day Calendar of March 1, 1933.

(Signed) CHAS. P. SMITH,
[SEAL.] *Member.*

APPENDIX A-5.

UNITED STATES BOARD OF TAX APPEALS.

Docket Nos. 14516, 14517, 42664.

BANKERS POCAHONTAS COAL COMPANY,
Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

Petitioner's Motion for Entry of Tax Determination With Supporting Statement and Argument.

(Filed May 19, 1933. Denied May 19, 1933.)

Petitioner, Bankers Pocahontas Coal Company, moves the Board:

1. To redeter the tax deficiencies for the calendar years 1920 to 1926, inclusive, herein in controversy, pursuant to the principles of the recomputation herewith tendered by petitioner, and marked for reference Exhibit "A", and for said purposes,

(*a*) To hold that under said mandate upon the record herein, and pursuant to the principles of *Murphy*

Oil Co. v. *Burnet, Commissioner,* decided previous to these cases, petitioner is entitled (1) to exclude in the several years from gross income the amounts therein received, purporting to be payments for tonnage of coal to be mined, but being in fact payments of bonus because said tonnage was not mined and the lessee lost the right to mine said tonnage under the contract therefor with petitioner, and (2) to use said payment as a credit of capital returned upon the basic content value of March 1, 1913, with a consequent recomputation and reduction of the depletion unit thereafter allowable, and for said purposes to state the capital tonnage content on March 1, 1913, to be 37,608,642 tons and the basic content value thereof to be $1,353,911.11 as determined of the record from stipulations of the parties.

(*b*) And for such other relief as may appear just and proper as incident to a true determination of the liability for tax deficiencies.

In support of said motion, petitioner by its attorney, respectfully would show the Board:

The Nature of the Controversy.

In *Murphy Oil Co.* v. *Commissioner,* 15 B. T. A. 1195, and *Bankers Pocahontas Coal Co.,* 18 B. T. A. 901, this Board held bonus royalties were non-depletable gross income upon authority of *Nelson Land & Oil Co.* v. *Commissioner,* 3 B. T. A. 315, decided upon the grounds that bonus payments by a lessee to a lessor constitute taxable income, and the Treasury Regulation that said bonus receipts were a return of capital was consequently invalid.

Upon cross-petition for review taken by respondent Commissioner to the Circuit Court of Appeals, Ninth Circuit, said Board decision in the Murphy Oil Company case was specifically reversed (55 Fed. (2) 17),

and upon petition for review by this petitioner to the Circuit Court of Appeals, Fourth Circuit, said Board decision in this Bankers Pocahontas Coal Company case was generally affirmed with no reference to the point (55 Fed. (2) 626).

The Supreme Court of the United States, having granted certiorari to the petitioners in each case, said herein (Record p. 187) in its order thereon:

> "The case (*Bankers Pocahontas Coal Co.* v. *Commissioner*) is assigned for argument immediately following Case No. 80, *Murphy Oil Co.* v. *Burnet, Commissioner of Internal Revenue.*" (Parentheses inserted.)

Both cases were argued on the same day and decided on the same day (Mr. Justice Stone writing). In the Murphy Oil case, decided first, the Circuit Court of Appeals was affirmed specifically, and the Treasury Regulation was approved. In the Bankers Pocahontas Coal case, three definite points were decided, none of which included said point decided in the Murphy Oil case, and the respective Circuit Court of Appeals was affirmed. Thus, the Murphy and Bankers cases apparently stand in conflict after their decision by the Supreme Court just as they did after decision by the Circuit Courts of Appeals, unless the mandate in the Bankers case is not inclusive of and decisive of the point concerning bonus payments specifically decided otherwise in the affirmance of the Murphy Oil case.

The Facts Herein as to Bonus and Basis Tonnage Content and Value.

Petitioner herein contested deficiency letters, holding it was a lessor and not a vendor of coal in place

under the laws of West Virginia, and allowing the statutory deduction as to a depletion unit of 3.6 cents per ton as derived from a valuation of 14,000,000 tons of recoverable coal existing on March 1, 1913, and having a capital value on that date of $510,000. By stipulated agreement of the parties it appeared the recoverable coal was 37,608,642 tons (Record, p. 43), whereby the value is $1,353,911.11 (Record, p. 53) as the return thereof at 3.6 cents per ton. These revised figures are properly to be substituted for the original figures in further consideration of the case.

The deficiency letters for 1924, 1925 and 1926 (Record, pp. 31, 33, 35) proposed depletion allowances upon coal paid for at separate depletion units computed as to each separate contract, and being somewhat less than 3.6 cents per ton, making the following explanation (Record, p. 31):

> Based on the terms of the leases in effect on March 1, 1913, the recoverable tonnages and productions, the following computations of values are in conformity with the regulations and are used instead of the $0.36 originally allowed.

This variance of depletion rate was substantially waived by a stipulation of parties that respondent allowed a depletion of $0.36 per ton (Record, p. 102).

The previous deficiency letters for 1920 to 1923, inclusive, (Record, pp. 12, 23) do not show the detail of depletion allowances, or the coal mined or paid for. The stipulated tonnages mined or paid for (Record, pp. 43-46) show some variations from the figures used in the deficiency letters for 1924-26.

Petitioner contested the deficiency letters before the Board only upon two grounds, (*a*) that its receipts constituted non-taxable income as the proceeds subsequently collected of sale-in-place contracts effected before the Amendment (Record, p. 7), and (*b*) if taxable income, that a greater depletion rate had been established in prior liquidation and should be used (Record, p. 8). Since depletion upon coal paid for was allowed in the letters, as stated above, and respondent Commissioner did not by affirmative answer seek to change the basis, depletion upon *coal mined* as distinguished *from coal paid for* was not in controversy. Details as to other points contested are here omitted as immaterial.

The evidence offered and Board findings thereon show its lessees paid petitioner (Record, p. 41) certain sums annually.

> * * * "as a minimum rental or royalty for the property herein demised, whether the quantity of coal mined shall produce that amount of royalty or not, but the Lessees shall have the privilege of mining the next succeeding year, free of royalty, a sufficient amount of coal above the amount necessary to produce the minimum royalty for that year to reimburse themselves for the deficiencies in the preceding year."

with the tonnage mined, the tonnage paid for, and the royalty receipts under each lease for the several years from 1913 to 1926 inclusive, and thereby that petitioner received bonus payments in substantial excess of payments for coal mined in the years in controversy (Particularly Leases No. 2 and No. 4, Record, pp. 44, 45),

which excess amounts petitioner claims are capital returns applicable in reduction of basic capital content with consequent readjustment of the depletion unit allowable for the ensuing year under the Murphy Oil case, and are not gross income not subject to depletion as previously held by the Board.

Although petitioner and respondent Commissioner were only in disagreement upon the two issues of whether the income was taxable at all or was subject to the larger depletion unit applied in previous litigation, the Board interjected and decided a third issue that bonus was gross income but not depletable whereby depletion was allowed only upon coal mined. The Board ruling that bonus is gross income not depletable is reversed by the Murphy Oil decision, and its application will properly dispose of the bonus payments in the present redetermination.

ARGUMENT.

The Existence of the Bonus Herein.

The equity of a lessor subject to depletion when leased on March 1, 1913, for the entire operating life of the property is the value on the basic date of "royalties and other payments to be expected under the terms of the lease in effect on that date" (Reg. 45, 62, 65, 69) (Art. 204(d)). The instant lease (quoted supra) deals with royalties and other payments, in that the minimum royalty is forfeit if equivalent coal is not mined.

A royalty is the retained interest of the lessor received as revenue (*Ferguson* v. *Commissioner*, 45 F. (8) 573, 577) and is measured by actual production (*Burnet* v. *Harmel*, 287 U. S. 103, 112). Hence the minimum not applied to coal mined is a bonus or premium.

The Mandate Does Not Exclude the Adjustment Sought.

The question here is not decided in the opinion of the Court.

In *Bramwell* v. *U. S. F. & G. Co.*, 269 U. S. 483, 489; 70 L. Ed. 368, 372, the Court says:

> "It is a rule of universal application that general expressions used in a court's opinion are to be taken in connection with the case under consideration."

Herein, the opinion says:

> "We granted certiorari on a petition which assails the judgment below on three grounds which will be separately considered."

But the petition for certiorari presented the bonus payments as governed by the Murphy Oil decision of the Circuit Court of Appeals, and did not present the third ground—the admissibility of evidence—considered and decided by the Supreme Court. It follows the bonus point, for consideration of which the case was probably originally advanced, is not passed on in the opinion, and it is not reasonably to be concluded the Supreme Court thereby purposed to deny herein the benefits of its affirmance of the Murphy Oil decision.

In *East Tennessee V. and G. R. Co.* v. *Interstate C. Com.*, 181 U. S. 1, 17, 45 L. Ed. 719, 725, concerning the construction to be given to its opinions, the Court says:

> "The language of the opinions which is relied upon must be read in connection with its context,

> and must be construed in the light of the issue which was in controversy in the cases and which was decided."

In *United States* v. *Mitchell,* 271 U. S. 9, 14, 70 L. Ed. 799, 802, it is said:

> "It is not to be thought that a question not raised by counsel or discussed in the opinion has been decided merely because it existed in the record and might have been raised and considered."

Application of the principles approved in the Murphy Oil case produces a reduction of the depletable capital content and a resulting smaller depletion unit. The rehearing applied for and denied by the Supreme Court does not address itself directly to the present question, it is submitted in overruling same, the Supreme Court has not foreclosed the point.

A Mandate is Subject to Construction.

In *Story* v. *Livingston,* 13 Pet. 358, 373, 10 L. Ed. 200, 207, we read:

> "The mandate is to be interpreted according to the subject matter to which it has been applied, and not in a manner to cause injustice."

In *West* v. *Brashear,* 14 Pet. 51, 54, 10 L. Ed. 350, 351, it is said:

> There has been some discussion at the bar as to the principles by which a circuit court of the United States is to be governed when executing a mandate from the Supreme Court. Undoubtedly the mandate must be its guide. It is the judgment of this Court transmitted to the Cir-

> cuit Court. And when the direction in the mandate is precise and unambiguous, it is the duty of the Circuit Court to carry it into execution, and not to look elsewhere for an authority to change its meaning. But, when as in this case, the Circuit Courts are referred to testimony to ascertain the amount to be decreed, and are authorized to take new evidence on the point, it may sometimes happen that there will be some uncertainty and ambiguity in the mandate; and in such a case, the Courts below have unquestionably the right to resort to the opinion delivered at the time in order to assist them in expounding it.

In *Board of Supervisors* v. *Kennicott,* 4 Otto 498, 24 L. Ed. 260, the mandate on the former appeal remanded the case "with directions to award a new trial," and that "further proceedings be had in conformity to the opinion and decree of this Court." After saying that technically there was no "new trial in equity," the Court proceeds:

> * * * "as our mandates are to be interpreted according to the subject matter of the proceedings here, and, if possible, so as not to cause injustice (*Story* v. *Livingston*) it is proper to inquire what must have been intended by the use of that term (new trial) in the decree, since it cannot have its ordinary meaning. For that purpose, we held, in *West* v. *Brashear,* that resort might be had to the opinion delivered at the time of the decree. * * * Under these circumstances, it is apparent that the words 'new trial' were used to convey the idea of such further action as should be found necessary to carry into effect what had already been decided."

In *Mitchel* v. *United States,* 15 Pet. 52, 84; 10 L. Ed. 658, 670, wherein it is said:

> "The meaning of the mandate may be ascertained from the instrument itself; but the reasons which induced the Court to make it, are to be found in the evidence contained in the original record. The Court will now do what it did in the case of *Sibbald* (12 Pet. 493). It said:
>
> " 'To ascertain the true intention of the decree and mandate of this Court, the decree of the Court below, and of this Court, and the petitioner's title, must be taken into consideration. In 10 Wheat. 431, this Court says: "The proceedings in the original suit are always before the Court, so far as to determine any new points between the parties." ' "

Respectfully submitted,

(S.) CAMDEN R. MCATEE,
Attorney for Petitioner.

APPENDIX A-6.

UNITED STATES BOARD OF TAX APPEALS.

Docket Nos. 14516, 14517, 42664.

BANKERS POCAHONTAS COAL COMPANY, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

EXHIBIT A.

Petitioner's Recomputation Proposal.

(Filed May 19, 1933. Denied May 19, 1933.)

Petitioner, Bankers Pocahontas Coal Company, herewith presents and moves for entry as a proper execution of the mandate herein of the following:

Plaintiff's Redetermination of Tax.

	Existing deficiency.	Herein.	Overassessment.
1920	$5,202.27	$493.30	$4,708.97
1921	7,849.75	None	7,849.75
1922	4,150.08	None	4,150.08
1923	4,102.78	34.24	4,068.54
1924	3,677.23	None	3,677.23
1925	6,855.09	3,795.36	3,059.73
1926	7,333.85	4,945.41	2,388.44

Supporting and Explanatory Schedules.

In the foregoing, the only change from respondent's recomputation is the exclusion from gross and net income of the excess of coal paid for each year over coal mined each year. Said excess is treated as a return of capital in reduction of basic capital content with consequent recomputation of the resulting depletion unit. This is pursuant to principles as affirmed in *Murphy Oil Co.* v. *Burnet,* 287 U. S. 299.

The figures used are derived from the record herein.

The net income for the several years is so revised as follows:

Year.	Board net income.		Less bonus.	Revised net income.
1920	$39,241.83	(1)	$24,416.20	$14,825.63
1921	47,067.66	(2)	42,261.64	4,806.02
1922	61,953.85	(3)	38,908.60	23,045.25
1923	58,569.32	(4)	33,520.80	25,048.52
1924	(8) 54,545.73	(5)	30,185.20	24,360.53
1925	52,731.44	(6)	25,840.40	26,891.04
1926	54,324.83	(7)	21,136.90	33,187.93

	(1) 1920		(2) 1921		(3) 1922	
	Tons.		Tons.		Tons.	
Lease 2	62,811	$6,281.10	65,340	$6,534.00	64,136	$6,413.60
3	.....	.....	1,712	119.84	.....	.....
4	13,082	1,308.20	74,852	7,485.20	.....	.....
	168,269	16,826.90	281,226	28,122.60	324,950	32,495.00
		$24,416.20		$42,261.64		$38,908.60

		(4) 1923.		(5) 1924.
Lease 2	68,587	$6,857.80	62,072	$6,207.20
Lease 4	266,630	26,663.00	239,780	23,978.00
		$33,520.80		$30,185.20

		(6) 1925.		(7) 1926.
Lease 2	51,196	$5,119.60	29,971	$2,997.10
Lease 4	207,208	20,720.80	181,398	18,139.80
		$25,840.40		$21,136.90

(8) Figure taken from respondent's present proposal.

	1920.		
Revised net income		$14,825.83	
Invested capital		$316,513.02	
Adjustments:			
Tax	$1,427.05		
Dividends	20,696.98		
		22,124.03	
		$294,288.99	
Deduction for Dividends:			
Available earnings		$14,825.83	
Tentative Tax		1,492.58	
(33.70)		13,333.25	
Dividend paid 3/31		7,500.00	
Earnings 90 days		3,033.00	
Paid from surplus		4,467.00	
Prorated 276 days			3,369.96
Dividend paid 5/10		22,500.00	
Earnings for 40 days		1,348.00	
Paid from surplus		21,152.00	
Prorated for 236 days			13,645.52
Dividend paid 6/30		9,000.00	
Earnings for 51 days		1,718.70	
		7,281.30	
Prorated 185 days			3,681.50
			20,696.98
Computation of tax:			
Excess profits tax			None
Balance		$14,825.83	
Exemption		2,000.00	
		12,825.83	$1,282.58
Previously assessed			789.28
Additional			$493.30

1921.

Revised net income		$4,806.02	
Plus depletion	$11,921.87		
Less revised depletion	10,312.61		
		1,609.26	
Taxable net income		6,415.28	
Profits tax		6,415.28	None
Balance		2,000.00	
		4,415.28	
10%			441.53
Previously assessed			698.95
Overassessment (barred)			257.42

1922.

Revised net income		$23,045.25	
Plus depletion	16,799.36		
Less revised depletion	16,112.46		
		686.90	
		23,732.15	
Tax 12½%			2,966.52
Previously assessed			3,594.13
Overassessment (barred)			627.61

1923.

Revised net income		25,048.52	
Plus depletion	17,090.60		
Less revised depl	16,118.04		
		972.56	
		26,021.08	
Tax 12½%			3,252.63
Previously assessed			3,218.39
Additional			34.24

1924.

Revised net income		$24,360.53	
Plus Depletion	20,553.41		
Less Revised Depl	18,498.07		
		2,055.34	
		26,415.87	
12½% tax			3,301.98
Previously assessed			7,235.40
Overassessment			3,933.42

1925.			
Revised net income		26,891.04	
Plus Depletion	18,851.47		
Less Revised Depl	16,547.40		
		2,304.07	
		29,195.11	
13% tax			3,795.36
1926.			
Revised net income		33,187.93	
Plus Depletion	22,547.56		
Less Rev. Depl	19,102.79		
		3,444.77	
		36,632.70	
Tax 13½%			4,945.41

Depletion Unit Recomputation.

		Base.	Reserves.	Rate.
March 1, 1913		1,353,911.11	37,608,642	.036
		93,741.50	2,881,708	
		1,260,169.61	34,726,934	.036
	16,423.02			
1920	24,416.20	40,839.23	456,195	
		1,219,330.38	34,270,739	.03505
	10,312.61			
1921	42,261.64	52,574.25	331,163	
		1,176,756.13	33,939,576	.0346
	16,112.46			
1922	38,908.60	55,021.06	465,649	
		1,121,735.07	33,473,927	.0338
	16,118.04			
1923	33,520.80	49,638.84	477,161	
		1,072,096.13	32,996,766	.0324
	18,498.07			
1924	30,185.20	48,683.27	570,928	
		1,023,412.86	32,325,838	.0316
	16,547.40			
1925	25,840.40	42,387.80	523,652	
		971,025.06	31,802,186	.0305
	19,102.79			
1926	21,136.90	40,239.69	626,321	
		930,785.37	31,175,865	

Respectfully submitted,

(s) CAMDEN R. MCATEE,
Attorney for Petitioner.

APPENDIX A-7.

UNITED STATES BOARD OF TAX APPEALS.

WASHINGTON.

Docket Nos. 14516, 14517, 42664.

BANKERS POCAHONTAS COAL CO., *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

DECISION.

(Entered May 19, 1933.)

The Board by its order of January 18, 1933, ordered the parties litigant on a day certain to present recomputations of tax for the calendar year 1924, pursuant to mandate received therefor from the Circuit Court of Appeals for the Fourth Circuit (as affirmed by the Supreme Court of the United States), affirming the determination of the Board for the years 1920 to 1926, inclusive, excepting the year 1924. The day certain for presentation thereof was continued from time to time by the parties with the approval of the Board and final hearing was had thereon on May 17, 1933.

The respondent has filed a recomputation thereof for said year 1924, pursuant to the opinion of the Circuit Court of Appeals and the affirmance, showing a total tax of $6,818.21 instead of $7,235.40 as heretofore determined and that thereby an overassessment and overpayment of $417.19 in favor of petitioner were properly to be awarded.

The petitioner has filed its motion for entry of its recomputation filed as part thereof for all years adopt-

ing respondent's recomputation for 1924 of net income as required to be made by the Circuit Court of Appeals, but seeks further adjustment of net income for each year by excluding therefrom such part of minimum royalty payments received as exceed the payment therefrom for coal actually mined by the lessees as representing bonus payments. Petitioner contends that the alleged bonus payments constitute a return of capital with a consequent reduction of the depletion unit allowable in the succeeding year as authorized by the decision and opinion of the Supreme Court in *Murphy Oil Co.* v. *Burnet,* 53 S. Ct. 161, and that under the opinion of the Supreme Court herein said adjustment is a part of a reasonable and just execution of the mandate herein.

After argument by respective counsel the motion of petition is denied and said computation of the petitioner is rejected, it appearing that the mandate of the Circuit Court of Appeals herein is not ambiguous in its terms.

The premises considered, it is

Ordered and decided that there are deficiencies in tax due from the petitioner as follows:

1920	$5,202.27
1921	7,849.75
1922	4,150.08
1923	4,102.78
1925	6,855.09
1926	7,333.85

and that there is an overpayment for the year 1924 to be refunded in the amount of $417.19.

(Signed) CHAS. P. SMITH,
[SEAL.] *Member.*

Certification for United States Board of Tax Appeals, Washington, as to Documents, Appendix A-4-5-6-7.

UNITED STATES OF AMERICA,
District of Columbia, ss:

I, B. D. Gamble, clerk of the United States Board of Tax Appeals, hereby certify the foregoing and attached to be true and correct copies of the petitioner's motion for entry of tax determination, with supporting statement and argument, petitioner's recomputation proposal, order dated January 18, 1933, and decision in Docket Number 42664, wherein Bankers Pocahontas Coal Company is Petitioner and the Commissioner of Internal Revenue is Respondent.

In testimony whereof I hereunto subscribe my name and affix the seal of said Board of Tax Appeals at the city of Washington in said District this 20th day of May, 1933.

[Seal U. S. Board of Tax Appeals.]

B. D. GAMBLE,
Clerk U. S. Board of Tax Appeals.

APPENDIX B.

Petitioner's method obtains the same taxable income from the property during its life as does the Board method, but with different allocations as in the several years.

For illustration assume a 4-year life; capital depletable value of $10,000, original coal content of 100,000 tons; original depletion rate of 10 cents per ton. Lessee is to pay $25,000 for 25,000 tons each year as a minimum payment under the same lease (quoted herein on pp. 7, 8), but mines respectively 20,000 tons the

first and second years; 25,000 tons the third year, and 35,000 tons the last year.

The Board computation of resulting net income:

Year.	Tons mined.	Tons paid.	(a) Depletion and (b) Capital return.		Non-depleted income.	De-pleted income.	Tax-able income.
(1)	20,000	25,000	(a)	$2,000	$5,000	$18,000	$23,000
			(b)	None			
(2)	20,000	25,000	(a)	2,000	5,000	18,000	23,000
				None			
(3)	25,000	25,000	(a)	2,500	.....	22,500	22,500
(4)	35,000	35,000	(a)	(3,500)	.....	31,500	31,500
		110,000		$10,000	$10,000	$90,000	$100,000

The petitioner's computation per Murphy Oil Co. Case:

Year.	Tons mined.	Tons paid.	(a) Depletion and (b) Capital return.		Non-depleted income.	De-pleted income.	Tax-able income.
(1)	20,000	$25,000	(a)	$2,000			
			(b)	5,000	.....	$18,000	$18,000
(2)	20,000	25,000	(a)	750			
			(b)	2,250	$2,750	19,250	22,000
(3)	25,000	25,000		.....	25,000	.....	25,000
(4)	35,000	35,000		.....	35,000	.....	35,000
	100,000	$110,000		$10,000	$60,750	$37,250	$100,000

The two schedules show the following:

In year 4, the lessee must pay a second time for $10,000 of coal paid for in years (1) and (2) because not mined within the contract time limit.

The Board treats the $10,000 as $5,000 of non-depletable income in year (1) and year (2) by reason of its prior decisions subsequently reversed by the *Murphy Oil case,* and allows depletion upon coal mined each year (item a).

Petitioner treats the $10,000 as a bonus capital return of $5,000 in year (1) and of $2,250 in year (2). Petitioner allows depletion upon coal mined each year but the capital return restores the basic capital in year (2). In other words, the Depletion and Capital

Return in year (1) is $7,000, after 20,000 tons are mined, whereby the remaining 80,000 tons are worth $3,000 or $0.0375 instead of 10 cents per ton. The Depletion in year (2) on 20,000 tons mined is $750, leaving $2,250 of capital value to be offset against the $5,000 of bonus capital return. This eliminates capital value and leaves $2,750 of said bonus as income because there is no capital value left. In years (3) and (4) the entire payments become non-depletable income subject to tax.

Under each computation the lessor receives $110,000, subject to a reduction of $10,000 of capital therein returned, and taxpays $100,000 during the life of the property.

Petitioner's method is that approved by *Murphy Oil Co.* v. *Burnet*, which rejects the other method.

Petitioner's method gives less taxable net income in the earlier years when higher tax rates prevail, and in this way lowers the tax for those years. It raises the tax in subsequent years by producing a larger taxable income.

SUPREME COURT OF THE UNITED STATES.

No. 104.—October Term, 1932.

Bankers Pocahontas Coal Company, Petitioner, *vs.* David Burnet, Commissioner of Internal Revenue.	On Writ of Certiorari to the United States Circuit Court of Appeals for the Fourth Circuit.

[December 5, 1932.]

Mr. Justice Stone delivered the opinion of the Court.

Petitioner, in 1912, acquired West Virginia coal lands in fee and, by assignment from the prior owners, certain leases or contracts entered into by them with various coal operators, by which the latter acquired the right to enter upon and use the lands for the production of coal and coke for a specified period, in consideration of stipulated royalties for the coal and coke produced, including minimum royalty payments in each year. In determining petitioner's income and profits taxes for the years 1920 to 1926, the Commissioner of Internal Revenue treated the royalty payments, after deducting a depletion allowance of 3.6¢ per ton of coal mined, as taxable income of petitioner, and assessed a corresponding increase in the tax. On appeal this ruling of the Commissioner was sustained, both by the Board of Tax Appeals, 18 B. T. A. 901, and the Court of Appeals for the Fourth Circuit, 55 F. (2d) 626. We granted certiorari, — U. S. —, on a petition which assails the judgment below on three grounds, which will be separately considered.

First. It is insisted that no part of the royalties is taxable income of petitioner. Petitioner rests this contention on what is stated to be a rule of law of West Virginia, that under coal leases, like those presently involved, the title to the coal, in place, passes to the lessee or operator immediately on execution of the lease. From this it is argued that the royalties received were but payments for capital assets acquired and sold ~~by petitioner~~ before the adoption of the Sixteenth Amendment, and that their taxa-

tion as income is not authorized either by the statute or by the Sixteenth Amendment, because not apportioned.

The question whether payments of bonus and royalties from the lessee to the lessor of an oil lease are income within the meaning of the Revenue laws taxing income, or a return of capital as upon a sale of the oil, was recently before this Court in No. 26, *Burnet* v. *Harmel,* decided November 7, 1932. Although it was contended there, as it is here, that by state law the title to the mineral content of the leased land passed to the lessee upon execution of the lease, it was held that this characterization of the transaction in the local law did not affect the conclusion that the payments were gross income subject to tax, after the deductions allowed by the taxing act. The considerations which led to the conclusion that bonus and royalties paid to the lessor of Texas oil lands are taxable income and not a conversion of capital, as upon a sale of capital assets, are equally applicable to West Virginia coal leases, whether the title to the coal passes to the lessee in place at the date of the lease, or only upon severance by the lessee.

The applicable statutes thus construed and applied do not tax any part of petitioner's capital investment before March 1, 1913. Section 234 (a) (9) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, and regulations under it, require depletion allowances upon bonus and royalty payments received by the lessor of mineral lands, sufficient to provide for a return in full of his invested capital. The provisions of that section, and the related Treasury Regulations have been continued with the later Revenue Acts, see No. 80, *Murphy Oil Co.* v. *Burnet,* decided this day. The fact that the depletion allowance under the Revenue Act of 1913 was more limited is not pertinent here. *Burnet* v. *Thompson Oil & Gas Co.,* 283 U. S. 301.

Second. In a suit brought by the petitioner in the District Court for Northern West Virginia, *Bankers Pocahontas Coal Co.* v. *White, Collector of Internal Revenue,* with respect to taxes for the years 1914 to 1919, it was held that petitioner was entitled to a depletion allowance on royalties received from the leases involved in the present suit, of 5¢ per ton of coal mined. It is insisted that the decision in that case was *res adjudicata* of that issue, and that in fixing the depletion allowance of the present case at 3.6¢ per ton, the court below and the Board of Tax Appeals erroneously refused

to follow the decision of the District Court in the earlier case. With respect to this contention it is sufficient to say that the suit in the District Court was not against the Commissioner of Internal Revenue, the respondent here, but against the Collector, judgment against whom is not *res adjudicata* against the Commissioner or the United States. *Graham & Foster* v. *Goodcell*, 282 U. S. 409, 430; *Sage* v. *United States*, 250 U. S. 33; see *Smietanka* v. *Indiana Steel Co.*, 257 U. S. 1; compare *Union Trust Co.* v. *Wardell*, 258 U. S. 537.

Third. After the Board of Tax Appeals had filed its findings of fact and opinion, both respondent and petitioner submitted recomputations of the amount of the deficiency under the Board's report, as provided by Rule 50 of the Board's Rules of Practice. In petitioner's recomputation, the claim was made for the first time that the minimum royalty payments stipulated by the leases had in some instances exceeded the amount of the per ton royalty which would have been payable on actual production, and it was asked that the depletion allowance be computed upon the basis of the actual payments made, instead of upon the number of tons extracted. Petitioner, at a hearing on the recomputation, tendered evidence in support of this claim. The Board rejected the evidence and denied petitioner's motion for a rehearing in order to present this contention. The court below upheld this action.

The Board is authorized to prescribe rules of practice and procedure for the conduct of proceedings before it. § 601, Revenue Act of 1928, c. 852, 45 Stat. 791, 871, 872, amending § 907 (a), Revenue Act of 1924, as amended; see *Goldsmith* v. *Board of Tax Appeals*, 270 U. S. 117. Rule 50 prescribes the procedure for computing the amount of the deficiency after the Board has heard and decided the issues raised and presented on the merits. In terms, it directs that the hearing on the computation which it authorizes is to be "confined strictly to the consideration of the correct computation of the deficiency or overpayment resulting from the determination already made, and no argument will be heard upon or consideration given to . . . any new issues". The Board has held that under the Rule new issues may not be raised and urged on a hearing upon the computation. *Great Northern Ry. Co.* v. *Commissioner*, 10 B. T. A. 1347, affirmed on other issues 40 F. (2d) 372. The rule was a proper exercise of the power of the Board to pre-

scribe the practice in proceedings before it. See *O'Meara* v. *Commissioner*, 34 F. (2d) 390, 395; *Boggs & Buhl* v. *Commissioner*, 34 F. (2d) 859, 861; *Metropolitan Business College* v. *Blair*, 24 F. (2d) 176, 178; compare *Sooy* v. *Commissioner*, 40 F. (2d) 634.

The purpose of the tendered evidence was to bring the case within the ruling of the Court of Appeals for the Ninth Circuit affirmed in No. 80, *Murphy Oil Company* v. *Burnet*, *supra*, that bonus payments to the lessor of a mineral lease are to be treated as advanced payments of royalties and depletion allowed. This was a new issue. We need not consider the contention of the government that it does not clearly appear either that the stipulated minimum payments exceeded the total per ton royalties upon the leases or that, even if they did, the excess of the minmum royalties over the royalties computed on actual production can, upon a proper construction of the leases, be treated as advance payment of the per ton royalties to accrue in future years. It is not shown that the evidence tendered was not available to the petitioner in ample time to present it before the Board had made and filed its findings of fact and opinion. Under the circumstances, we cannot say that the Board abused its discretion in denying a rehearing.

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.

SUPREME COURT OF THE UNITED STATES.

No. 105.—October Term, 1932.

D. J. F. Strother, Petitioner,
vs.
David Burnet, Commissioner of Internal Revenue.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Fourth Circuit.

[December 5, 1932.]

Mr. Justice Stone delivered the opinion of the Court.

The decision in this case, which is here on certiorari, — U. S. —, turns on that in No. 104, *Bankers Pocahontas Coal Co., Petitioner* v. *Commissioner of Internal Revenue,* just decided.

Petitioner, a stockholder in the Bankers Pocahontas Coal Co., received dividends upon his stock which were, to some extent, a distribution of the royalty payments received by the corporation and involved in its suit against the Commissioner. The ruling of the Commissioner in this case, that the amounts so distributed from royalties were taxable income, was upheld by the Board of Tax Appeals, 18 B. T. A. 901, and by the Court of Appeals for the Fourth Circuit, 55 F. (2d) 626, which remanded the case to the Board for further proceedings, to enable the petitioner to offer additional testimony having a bearing on the correct computation of the deficiency, in accordance with the opinion of the court. The parties stipulate that the decision of this case shall be controlled by that of *Bankers Pocahontas Coal Co.* v. *Commissioner of Internal Revenue,* and the judgment below is accordingly

Affirmed.

A true copy.

Test:

Clerk, Supreme Court, U. S.